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OIG's Semiannual report covering the period April 1 2001 - September 30, 2001

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[FDIC OIG Semiannual Report cover: Image of U.S. flag]
Semiannual Report to the Congress, April 1 2001 - September 30, 2001

Inspector General's Statement

The nation continues to cope with the tragic events of September 11, 2001 and their aftermath. We, with the nation, mourn the loss of life and offer our sympathy to the victims' families and friends. Notwithstanding the deep sorrow we all feel, the profound expressions of patriotism generated by the events of that day remind us that we are privileged to be public servants. Mindful of that privilege, the Federal Deposit Insurance Corporation (FDIC) Office of Inspector General (OIG) has recommitted itself to serving the American people and assisting the Corporation as it seeks to promote and maintain stability and public confidence in the nation's banking system. We are especially proud of members of our investigative staff who volunteered to assist with law enforcement activities at the site of the World Trade Center in New York City and at the Pentagon.

The OIG has been marked by other significant changes during the reporting period as well. These changes are organizational in nature and impact our work on a daily basis. The Corporation's 17th Chairman, Donna Tanoue, left office in July 2001 and Donald E. Powell assumed responsibility as the 18th Chairman of the FDIC on August 29, 2001. Within the OIG, Mr. Russell Rau, formerly with the National Aeronautics and Space Administration OIG, assumed the position of Assistant Inspector General for Audits on May 29, 2001 and a reorganization of the Office of Audits followed. Additionally the OIG created a new office, the Office of Policy Analysis and Congressional Relations, to provide the Congress and FDIC management with analyses of policy issues affecting the Corporation and the financial services industry. With these organizational changes we believe we are better positioned to add value to the Corporation and fulfill our reporting responsibilities to both the Chairman and the Congress.

Our work during the reporting period has not equaled the productivity levels of earlier semiannual reporting periods, partially owing to the reorganization of our Office of Audits and corresponding changes in audit processes and expectations. Additionally, the failure of Superior Bank, F.S.B., Hinsdale, Illinois, with estimated losses ranging from \$450 to \$550 million has impacted the FDIC OIG's work plan and products. To respond to a congressional request that we review various aspects of the Superior Bank failure, we delayed a number of ongoing assignments to focus on Superior as a priority. As of the close of the reporting period, we had five assignments ongoing related to that failure, the results of which will be discussed in our next semiannual report.

The OIG also devoted a significant level of resources during the reporting period to another priority project, our *Independent Evaluation of the FDIC's Information Security Program Required by the Government Information Security Reform Act*, and we issued a comprehensive report to management based on that work. Overall, and as discussed further in this semiannual report, we concluded that there is limited assurance that the Corporation has

established and implemented an overall information security program that provides adequate security. Given the significance of ensuring security of information resources at the FDIC, we will continue to work with management as it responds to the concerns we raised. We will also use the results of our review to identify more specifically those areas where our audit resources should be directed going forward. With respect to heightened security concerns overall, we have initiated a review of the physical security of FDIC facilities and will coordinate closely with the Corporation in its ongoing efforts to ensure the safety of all FDIC employees and visitors to corporate locations.

Shortly before I wrote this statement, our office held a week-long conference in Portsmouth, Virginia, the theme of which was Putting People First. Who can deny the importance of that message, given the thousands of lives so senselessly lost on September 11? This conference emphasized the value that the OIG places on its human capital and called upon OIG staff to become a high-performance organization, understand personality differences, embrace diversity, and practice Steven Covey’s seven habits of highly effective people.

A highlight of our conference was a presentation made by FDIC Director John M. Reich who spoke of the pressing issues facing the Corporation and, on behalf of the new Chairman, extended to the OIG an offer to engage in a partnership to address these challenges. The OIG eagerly accepts the opportunity extended by Director Reich to solidify our working relationships with the Corporation as we continue to serve the FDIC, the Congress, and the American people.

We have seen how one day can dramatically and irrevocably change the world. The future is also uncertain. The FDIC OIG will work tirelessly to preserve the public trust and looks forward to joining with the Corporation, the Congress, and the entire Inspector General community as we serve the country and honor the memory of those who lost their lives on September 11.

Gaston L. Gianni, Jr.

Inspector General

October 31, 2001

[Banner of American Flag precedes table of contents]

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[Overview banner with I Pledge Allegiance Insert precedes Major Issues section]

[Major Issues Section]

The Major Issues section of our report focuses on key challenges confronting the FDIC as it works to accomplish its mission. In the OIG’s view, these major issues fall into two broad categories. First, the Corporation faces challenges related to its core mission of contributing to the stability and public confidence in the nation’s financial system by insuring deposits, examining and supervising financial institutions, and managing receiverships. Such challenges sometimes involve significant policy decisions and are often influenced by external factors such as industry events, economic trends, activities of other federal banking regulators, consumer concerns, and congressional interest.

Second, a number of important operational matters require the Corporation’s attention as its workforce actually carries out the corporate mission. These issues touch on, for example, information technology resources and security, contracting activities, human capital concerns, cost efficiencies, and performance measurement and accountability.

We are also identifying an important emerging management challenge that warrants attention: security. This area extends beyond information resources security concerns to issues of personal security and safety, largely in response to the terrorist activities of September 11, 2001.

With respect to the first category, the Corporation must address risks to the insurance funds in a complex global banking environment that continues to experience change and offer expanded services. At the same time, the Corporation is charged with effectively supervising the financial institutions it regulates and carefully protecting consumers’ rights. A Board of Directors operating at full strength is essential to lead the Corporation as it faces such challenges. As the Corporation moves forward, the deposit insurance reforms initially proposed by former Chairman Tanoue will continue to be debated and deliberated by the banking industry and the Congress. One aspect of such reform involves the possible merger of

the Bank Insurance Fund and the Savings Association Insurance Fund, an action that the OIG supports. As our report discusses, we also believe that when such a merger occurs, the timing is opportune for the OIG to become the auditor of record for the Corporation. Our cooperative work with the U.S. General Accounting Office on the Corporation's financial statement audit is designed to see to that end.

Turning attention to the Corporation's more "operational" demands, the use of information technology (IT) at the FDIC is crosscutting and absolutely essential to the Corporation's accomplishment of its mission. In conducting its IT activities, the Corporation's priority must be the effective and efficient use of IT to achieve program results corporate-wide. It also needs to follow sound system development life cycle procedures, comply with IT principles espoused by legislation and regulation, and ensure that effective controls are in place and implemented to safeguard system security, mitigate risks, and protect IT resources. Given the extent of the FDIC's contracting activities, strong controls and vigilant contractor oversight are also critical to the Corporation's success. Contracting must be done in the most cost-effective manner. The Corporation's contract oversight mechanisms must protect the FDIC's financial interests and help ensure that the FDIC is actually getting the goods and services for which it is spending millions of dollars.

Major downsizing over the past 5 years and natural attrition have greatly impacted the FDIC workplace. As a result, the Corporation has lost leadership and, in some cases, expertise and historical knowledge. The Corporation's continuous diversity efforts, retraining and leadership programs, and redeployments are helping to restore some of the lost talent and skill. The FDIC must build on ongoing initiatives and continue to develop a comprehensive, integrated approach to human capital issues. It has worked with a contractor to help develop a process for a human capital strategy; however, the issue of human capital needs sustained attention.

In light of changes in the banking industry, advances in technology, and such dramatic shifts in staffing and skill levels, the Corporation has begun to closely scrutinize its business processes and their associated costs in the interest of identifying operational efficiencies. Among other activities, its Division of Supervision Process Redesign project, review of administrative services functions, and focus on the corporate planning cycle have generated new ideas for such efficiencies and are positive steps.

Finally, under the provisions of the Government Performance and Results Act with its emphasis on accountability, for all of these major issues and their corresponding challenges the Corporation must establish goals, measure performance, and report on its accomplishments.

Our Major Issues section also discusses the OIG's completed and ongoing/planned work to help the Corporation successfully confront these major issues and their associated challenges. We discuss areas where we identified opportunities for improvements and the recommendations we made in those areas. We made 34 nonmonetary recommendations during the reporting period. Our work targets all aspects of corporate operations and includes a number of proactive approaches and cooperative efforts with management to add value to the FDIC (see pages 11-24).

[Investigations]

The operations and activities of the OIG's Office of Investigations are described beginning on

page 25 of this report. As detailed in the Investigations section, the Office of Investigations is reporting fines, restitution, and recoveries totaling approximately \$11.8 million. Cases leading to those results include investigations of bank embezzlement, insider trading, bank fraud, misrepresentations regarding FDIC insurance, credit card fraud, securities fraud, and concealment of assets. Some of the investigations described reflect work we have undertaken in partnership with other law enforcement agencies and with the cooperation and assistance of a number of FDIC divisions and offices. To ensure continued success, the OIG will continue to work collaboratively with FDIC management, U.S. Attorneys' Offices, the Federal Bureau of Investigation, and a number of other law enforcement agencies (see pages 25-31).

[OIG Organization]

The OIG Organization section of our report highlights several key internal initiatives that we have actively pursued during the reporting period. The OIG's internal focus has been on achieving a higher level of performance, putting technology to work, and aligning human resources to support the OIG mission. This section of our report also references some of the cooperative efforts we have engaged in with management during the reporting period, including making presentations at corporate conferences and meetings. We present a discussion of proposed or existing laws and regulations reviewed during the past 6 months, refer to litigation efforts of OIG Counsel, and also capture some of our other internal initiatives this reporting period. In keeping with our goal of measuring and monitoring our progress, we visually depict significant results over the past five reporting periods (see pages 32-39).

[Appendix: Panel containing text "To The Flag of the United States of America" with faded image of U.S. flag as background]

We list the Inspector General Act reporting requirements and define some key terms in this section. The appendixes also contain much of the statistical data required under the Act and other information related to our work this period (see pages 42-49).

Highlights

- The Office of Audits issues a total of 9 reports and 11 other audit- or evaluation-related products.
- OIG reports include 39 nonmonetary recommendations to improve corporate operations. Among these are recommendations to strengthen Receivership Liability System security reviews and procedures, further progress on the Institution Data Management Project, and improve the Corporation's background investigation process for prospective and current employees.
- OIG investigations result in 18 indictments/informations; 10 convictions; and approximately \$11.8 million in total fines, restitution, and asset forfeitures.
- The OIG reviews 3 proposed or existing federal regulations and legislation and 22 proposed FDIC policies and directives and responds to 4 requests and appeals under the Freedom of Information Act and Privacy Act.
- The OIG continues efforts with the Division of Resolutions and Receiverships (DRR) to

pursue court-ordered restitution. As of September 30, 2001, the OIG is conducting 39 investigations that are being coordinated with DRR and involve a total of over \$1.2 billion in outstanding restitution orders or other types of debt.

- The OIG and U.S. General Accounting Office continue their joint effort to audit the Corporation's financial statements. The OIG plays an increasingly greater role in anticipation of assuming full responsibility for the audit.
- OIG counsel litigates 13 matters during the reporting period and provides advice and counsel on a number of issues.
- The OIG coordinates with and assists management on a number of initiatives, including its contractor oversight summit, Division of Supervision (DOS) training sessions on white-collar crime, briefing congressional staff on a criminal investigation related to a community bank, and participating at the Legal Division's Professional Liability and Financial Crimes Unit's continuing legal education program.
- The OIG accomplishes a number of internal office initiatives, including establishing an Electronic Crimes Team, furthering efforts to automate OIG workpapers, participating in interagency Government Performance and Results Act interest groups, engaging in a number of diversity activities, appointing an Information Security Manager, and launching a telework program.
- The OIG provides briefing information to Donald E. Powell, the new FDIC Chairman, to familiarize him with the role and mission of the OIG at the FDIC.
- The OIG participates actively in the DOS Process Redesign project to improve current operating efficiency and proactively prepare for challenges ahead. OIG staff are recognized by DOS for providing assistance.
- The OIG continues work to review the FDIC's special examination authority and DOS's effectiveness in monitoring risks posed by the nation's largest banks.
- The OIG's Office of Investigations responds to requests for assistance in terrorist investigations. Work is carried out in New York City and at the Pentagon. The OIG is also assisting the Federal Bureau of Investigation's Financial Crimes Unit in investigating the funding used to perpetrate the acts of terrorism on September 11 and links to possible future acts.
- The OIG initiates five reviews, several based on a congressional request, related to the failure of Superior Bank, F.S.B., Hinsdale, Illinois. Loss estimates resulting from the failure range from \$450 to \$550 million.
- The OIG issues the results of its *Independent Evaluation of the FDIC's Information Security Program Required by the Government Information Security Reform Act*. We conclude that there is limited assurance that the Corporation has established and implemented an overall information security program that provides adequate security.
- The OIG provides the results of analyses of the FDIC's 2000 performance measures to Congressman Dan Burton, Chairman of the Committee on Government Reform, U.S. House

of Representatives.

- The OIG conducts four evaluation projects in the major issue area of containing costs and assessing business processes at the FDIC: *Field Office Cost, Space Utilization, Design, and Usage*; the *FDIC's Long-Term Headquarters Housing Study*; the *FDIC's Corporate Planning Cycle* (conducted jointly with the Office of Internal Control Management); and *Study of Internal Control and Internal Review Programs*.
- The OIG begins an evaluation of the adequacy of the physical security of FDIC facilities in major cities and other selected sites.
- The OIG issues the results of its review of *the FDIC's Background Investigation Process for Prospective and Current Employees*; FDIC management takes prompt action in response. This review was requested by Sue W. Kelly, Chairwoman, Subcommittee on Oversight and Investigations, Committee on Financial Services, U.S. House of Representatives.
- As a result of OIG investigative efforts conducted with the Federal Bureau of Investigation, the Internal Revenue Service, U.S. Attorney's Office for the Southern District of West Virginia, and the U.S. Department of Justice, four more defendants enter guilty pleas related to an ongoing bank fraud investigation involving the First National Bank of Keystone.
- Mr. Russell A. Rau joins the OIG as Assistant Inspector General for Audits. The Office of Audits undergoes reorganization and a new Office of Policy Analysis and Congressional Relations is established.
- The OIG begins to develop a Human Capital Strategic Plan to align human resources policies and practices to support the OIG mission.
- The OIG completes planning efforts for an office-wide conference, the theme of which is *Putting People First*, scheduled for late October 2001.
- Two OIG teams are selected to receive Awards of Excellence from the President's Council on Integrity and Efficiency. Assistant Inspector General Russell A. Rau is selected to receive an Award for Excellence for exemplary leadership and service to the Inspector General community as Chair of the Federal Audit Executive Council.

[Major Issues Section preceded by panel containing faded U.S. flag overlaid with the following text - "and to the Republic for which it stands"]

Major Issues

The FDIC and the banking industry are experiencing significant and rapid change. We believe a number of issues associated with these changes are deserving of special attention at this time. These broad major issues are identifying areas where the OIG focuses its resources.

Organizational Leadership

The most significant event impacting the FDIC's organizational leadership during the reporting period involved changes in uppermost management at the FDIC. On June 12, 2001 Chairman Tanoue announced that she had submitted her resignation as Chairman effective

July 11, 2001. Director John M. Reich then served as Acting Chairman during an interim period that ended on August 29, 2001 when Donald E. Powell took the oath of office as the FDIC's 18th Chairman. Chairman Powell will encounter historical leadership challenges at the FDIC and a number of new ones as well. To illustrate, shortly after taking office, and in light of the terrorist events of September 11, 2001, Chairman Powell faced the inevitable inquiries on the effects of the events of that day on federal deposit insurance. The Corporation's response was firm, as indicated in a September 12, 2001 press release: "The public can rest assured that deposit insurance is in full force— money is safe in an FDIC-insured account." Strong leadership has always been vital in the banking and financial services industry. During the 1990's one or more Presidentially appointed positions on the Board of Directors frequently were vacant. Perhaps now more than ever, the Corporation needs a full complement of Board members to carry out the FDIC mission.

James Gilleran of California has been nominated to head the Office of Thrift Supervision, and the current Director, Ellen Seidman, has indicated that she will step down upon his confirmation. Anticipating the arrival of Chairman Powell at the FDIC and acknowledging the importance of continuity and sustained leadership, Director and then Acting Chairman Reich stated the following in a July 2001 speech before an Ohio/West Virginia Bankers Association meeting: "Once we've passed through this transition period, I believe the FDIC Board will enter a sustained period of stability."

Notwithstanding the recent or anticipated changes in the make-up of FDIC leadership, the Board continues to operate with one vacancy. The Board position of Vice Chairman has been vacant since January 2001. The FDIC is both the independent regulator of a significant portion of the nation's banking system, as well as the only federal insurer of deposits wherever placed in our nation's banks. As a corporation governed by its Board of Directors, the vital balance between various interests implicit in the Board's structure is preserved only when all vacancies are filled. Accordingly, we have strongly urged that vacancies on the FDIC's Board be filled as promptly as practicable in order to afford the FDIC the balanced governance and sustained leadership essential to the agency's continued success.

[Contained in the Major Issues section of the report is a panel containing information on Management Challenges at the FDIC.]

[Start of Management Challenges at the FDIC panel]

Management Challenges at the FDIC

In the interest of improving federal performance government-wide, the Senate Governmental Affairs Committee has asked Offices of Inspector General to identify the 10 most significant management challenges facing their agencies. At the FDIC, our office has identified and previously reported these challenges as follows:

- Organizational Leadership
- Supervising Insured Institutions
- Protecting Consumer Interests

- Addressing Risks to the Insurance Funds
- Merging the Insurance Funds
- Managing Information Technology
- Ensuring Sound Controls and Oversight of Contracting Activities
- Establishing Goals and Measuring Results
- Addressing Human Capital Issues
- Containing Costs and Assessing Business Processes

The Government Performance and Results Act provides a mechanism to establish goals and measures to address these significant management challenges. Through continuous Results Act reporting, the FDIC should address congressional expectations that the FDIC's performance and reports clearly inform the Congress and the public of the results and outcomes of the Corporation's major programs and activities.

An additional, rapidly emerging management challenge is overall security at the Corporation. This challenge encompasses not only information resources security, which we currently capture under Managing Information Technology, but also multiple aspects of physical security and personnel security which we discuss on page 24 of this report. While we have begun work in these areas, we anticipate that in the upcoming weeks the OIG will intensify its efforts and devote additional resources to all of the security matters referenced above. The Corporation has recognized the importance of these areas and is taking swift, proactive actions to address them. We will continue to work with the Corporation to protect and safeguard the people and the resources of the FDIC.

The OIG will continue to work closely with corporate management to address all of these challenges and will monitor progress made by the Corporation to fully conform with the intent of the Results Act.

[End of Management Challenges at the FDIC panel]

[The following is a continuation of the Major Issues section]

The OIG continues to emphasize its belief that to handle the challenges and issues facing the Corporation, a Board of Directors operating at full strength must be in place.

Supervising Insured Institutions

As the primary federal regulator of state-chartered institutions which are not members of the Federal Reserve System, the FDIC shares joint responsibility with the state banking departments for monitoring and supervising the safety and soundness of over 5,000 financial institutions. The challenge to the Corporation is to ensure that its system of supervisory controls will identify and effectively address financial institution activities that are unsafe, unsound, illegal, or improper before the activities become a drain on the deposit insurance funds.

Emerging trends and new developments in the banking industry will require the Division of Supervision (DOS) to increase its efforts to identify and assess risks from:

- subprime lending;
- declining underwriting standards for commercial real estate lending;
- rapid changes in bank operations between safety and soundness examinations;
- the growth of information technology and its increasing impact on payment systems and other traditional banking functions;
- fraudulent activities, which have contributed significantly to bank failures in recent years; and
- expanded banking activities permitted by the Gramm-Leach-Bliley Act.

Further, DOS may have to reevaluate the concepts of risk, capital, and asset valuation in light of recently developing investment products and methods.

There are also continuing pressures for the FDIC to increase the efficiency of the bank examination process designed to identify and assess these risks. Additionally, with the possibility of an economic downturn, DOS should assess its size and mix of expertise and skills in its workforce to ensure sufficient capacity for addressing increased risks. Considering the lead time required for developing new commissioned examiners, the FDIC needs to ensure the examination force will be adequate for handling potential problems and bank failures.

The OIG's work related to the Corporation's supervision activities during the reporting period consisted in part of ongoing assistance provided to the DOS Process Redesign Project. OIG staff provided input and feedback to proposals and questions and performed various research tasks. DOS acknowledged that the impact of their efforts would undoubtedly improve the division's operational efficiency.

Additionally, ongoing OIG work in the supervision area includes DOS monitoring of bank corrective actions, effectiveness of off-site monitoring tools, and Gramm-Leach-Bliley Act safety and soundness issues for state non-member banks.

Protecting Consumer Interests

The FDIC is legislatively mandated to enforce various statutes and regulations regarding, for example, consumer protection and civil rights with respect to state-chartered, non-member banks and to encourage community investment initiatives by these institutions. Some of the more prominent laws and regulations in this area include the Truth in Lending Act, Fair Credit Reporting Act, Real Estate Settlement Procedures Act, Fair Housing Act, Home Mortgage Disclosure Act, Equal Credit Opportunity Act, and Community Reinvestment Act (CRA) of 1977. The FDIC's primary means of accomplishing these tasks is through compliance examinations and CRA performance evaluations.

The FDIC must detect and promptly correct problems in institutions, promote compliance with consumer protection laws and regulations, and increase public understanding of and

confidence in the deposit insurance system. The FDIC must also respond to consumer complaints and inquiries related to consumer protection laws and regulations and deposit insurance coverage. Some recent concerns relate to financial literacy and predatory lending. These practices often seem to have a disproportionately negative effect on under-served low- and moderate-income borrowers, minority groups, and the elderly, who may be made vulnerable by a lack of credit availability, financial expertise, and financial counseling, or poor credit history.

Another important aspect of protecting consumer rights is consumer privacy. With the enactment of the Gramm-Leach-Bliley Act, the FDIC, along with other financial institution regulators, must work with the institutions to develop programs to ensure the privacy of consumer information.

In addition, based on our past work in DCA, we believe Division management must continue to improve controls over the CRA evaluation process to ensure that CRA examination procedures are applied on a consistent basis. FDIC management completed a comprehensive review of CRA reports from FDIC regions in December 2000. The Division is instituting new controls and procedures to address the concerns raised by both the OIG's work and the Division's own review.

The OIG's ongoing work related to "Fair Lending" reached its conclusion during the reporting period and we prepared our draft findings for management. Fair lending is a term used to describe compliance with two federal laws prohibiting discrimination in lending: the Fair Housing Act enacted by Title VIII of the Civil Rights Act of 1968 and the Equal Credit Opportunity Act of 1974. Our audit assessed (1) the FDIC's implementation of the 1999 Federal Financial Institutions Examination Council's (FFIEC) Interagency Fair Lending Examination Procedures as they relate to identifying fair lending risks during the off-site pre-examination planning phase of the fair lending reviews and (2) the related DCA management controls. The full results of our work will be discussed in our next semiannual report.

Addressing Risks to the Insurance Funds

A primary goal of the FDIC under its insurance program is to ensure that its deposit insurance funds remain viable. Achievement of this goal is a considerable challenge, given that the FDIC supervises only a portion of the insured depository institutions. The identification of risks in non-FDIC-supervised institutions requires coordination with the other federal banking agencies. The FDIC engages in an ongoing process of proactively identifying risks to the deposit insurance funds and adjusting the risk-based deposit insurance premiums charged to the institutions. The Division of Finance completes the final phase in this ongoing process by collecting the premium assessments.

Although the FDIC has a continuous program to ensure the viability of the deposit insurance funds, recent trends and events are posing additional risks to the funds. The economic landscape changed significantly following the events of September 11 and the potential exists for an increased number of bank failures. Additionally, the environment in which financial institutions operate is evolving rapidly, particularly with the acceleration of interstate banking, new banking products and asset structures, electronic banking, and consolidations that may occur among the banking, insurance, and securities industries resulting from the enactment of the Gramm-Leach-Bliley Act.

[Contained in the Major Issues section of the report is a panel titled - "OIG Focuses Resources on Priority Work: Failure of Superior Bank"]

[Start of OIG Focuses Resources on Priority Work: Failure of Superior Bank panel]

OIG Focuses Resources on Priority Work: Failure of Superior Bank

Upon the failure of Superior Bank, F.S.B. (Superior), Hinsdale, Illinois, the Office of Thrift Supervision closed the institution on July 27, 2001. At the time of closure, Superior had total assets of \$2.3 billion and total deposits of \$1.6 billion. The FDIC was named conservator and transferred the insured deposits and substantially all of the assets of Superior to Superior Federal, F.S.B. (New Superior), a newly chartered, full-service mutual savings bank. The failure of Superior will likely be one of the costliest of all recent failures. The FDIC's most recent loss estimate is between \$450 million and \$550 million. Superior Bank is the third FDIC-insured failure of the year, but the first institution insured by the FDIC's Savings Association Insurance Fund (SAIF) to be closed in 2001.

The OIG received a request from Senator Paul Sarbanes, Chairman of the Senate Committee on Banking, Housing, and Urban Affairs related to the failure of Superior Bank. Senator Sarbanes' request letter cited the magnitude of the potential loss to the SAIF at \$500 million, or 35 percent of the savings institution's assets. Given the FDIC's role in promoting and preserving public confidence in financial depository institutions, Senator Sarbanes requested that the OIG review why the failure of Superior Bank will result in such a significant loss to the insurance fund and that we make recommendations for preventing any such loss in the future. The Senator's request contained a list of specific issues for us to address. Because Superior Bank is an institution regulated by the Office of Thrift Supervision, the Department of the Treasury OIG has been asked to conduct a parallel review, as has the U.S. General Accounting Office. The Treasury OIG is also responsible for conducting a material loss review of Superior. We arranged to meet early-on with the Treasury OIG and GAO to coordinate work on these matters.

Further, in addition to Senator Sarbanes' request, we have initiated reviews to address four related issues surrounding the failure of Superior:

- The effectiveness of Section 38 of the Federal Deposit Insurance Act entitled "Prompt Corrective Action" in preventing or reducing losses to the deposit insurance funds as a result of bank failures;
- The processes in place that help ensure that Division of Supervision Case Managers stay informed of emerging issues to maintain an informed position on their caseloads and effectively monitor risk. The work will include identifying instances in which the case manager's evaluation of an institution differs substantially from that of its primary regulator;
- The FDIC's least cost decision to place Superior Bank into a conservatorship and its liquidation of remaining receivership assets; and
- The Division of Resolutions and Receiverships' marketing and resolution of Superior Federal, F.S.B. (New Superior).

To reduce the burden on corporate staff and avoid duplication of efforts, the OIG is

coordinating each agency's and each audit team's efforts to obtain documents and speak with FDIC personnel to the greatest extent possible. We expect to complete all of these efforts by the end of the next semiannual reporting period and will include our results in our next semiannual report.

[End of OIG Focuses Resources on Priority Work: Failure of Superior Bank panel]

[The following is a continuation of the Major Issues section]

The recent spate of bank mergers has created "megabanks," (sometimes referred to as "large banks") and, for many of these institutions, the FDIC is not the primary federal regulator. As of March 31, 2001, there were 38 megabanks in the country. Of the

\$5.3 trillion consolidated assets controlled by the 38 megabanks, the FDIC is the primary federal regulator for only \$162.5 billion in 3 institutions. The megabanks created as a result of mergers and the new or expanded services that the institutions can engage in under the Gramm-Leach-Bliley Act will no doubt present challenges to the FDIC and may pose new risks to the deposit insurance funds.

Back-Up Examination Authority

The authority to conduct a special examination of an institution regulated by the Office of the Comptroller of the Currency, the Office of Thrift Supervision, or the Federal Reserve Board should the FDIC independently conclude that institution poses a significant risk to the insurance fund, can only be invoked at the Board level. To monitor the insurance risks associated with the more than 4,000 institutions supervised by other federal banking agencies, the FDIC relies primarily on the examination and supervision provided by the other agencies. However, the Federal Deposit Insurance Act also provides the FDIC with the authority to conduct its own special examinations for insurance purposes and to take supervisory enforcement actions as needed to address safety and soundness concerns that increase risks to the funds.

Based on recent audit work assessing the FDIC's supervision for insurance purposes, we have identified several areas in which DOS needs additional emphasis and support in its interagency coordination efforts. Specifically, the FDIC needs to take action to ensure:

- the adequacy of interagency coordination arrangements, with respect to both information-sharing and attendance at key meetings with bank management;
- full access to the bank information systems developed and relied upon by the other federal banking agencies; and
- increased coordination with both federal and state regulators of securities and insurance operations.

We are in the process of updating work addressing these specific issues and anticipate reporting our results by the end of the calendar year. Additionally, our ongoing work related to the failure of Superior Bank will likely identify matters related to back-up examination

authority.

Merging the Insurance Funds

The FDIC and a number of other policymakers have proposed that the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF) be merged. In February 2000, Chairman Tanoue testified before the House Subcommittee on Financial Institutions and Consumer Credit on behalf of the FDIC regarding the merger of the funds. At that time, legislation (H.R. 3899) that would address the merger issue was introduced by House members Roukema and LaFalce.

Although the proposed legislation was not enacted, the FDIC continued to recommend the merging of the funds and encouraged debate in an effort to develop an industry consensus regarding the best approach to deposit insurance reform. On April 5, 2001, the Corporation released its report on recommendations to reform the federal deposit insurance system and, in addition to continuing to recommend the merger of the BIF and SAIF, recommended the following:

- Charge risk-based premiums to all institutions, regardless of the fund's size;
- Allow the insurance fund to build or shrink gradually around a target or range;
- Establish rebates that are based on past contributions to the fund; and
- Index insurance coverage to the Consumer Price Index to maintain its real value.

According to a corporate press release, the FDIC recommendations are not intended to significantly alter costs for insured institutions; instead, they are designed to spread out the costs more evenly over time and more fairly across banks. These recommendations are interrelated and should be implemented as a package, because piecemeal implementation could introduce new distortions and aggravate the problems the recommendations are designed to address.

To update: Subsequent to the end of this semiannual reporting period, on October 17, 2001, Chairman Powell testified on deposit insurance reform before the Subcommittee on Financial Institutions and Consumer Credit, Committee on Financial Services, U.S. House of Representatives. He supported the FDIC's report and recommendations as "a model for how agencies should create public policy proposals."

The Chairman recommended assessment credits rather than rebates and also recommended indexing for inflation from the date of enactment as well as higher coverage for retirement accounts. The Chairman believes the Congress has an excellent opportunity to remedy flaws in the deposit insurance system before those flaws cause actual damage either to the banking industry or the economy as a whole. While the Chairman believes we should remain flexible regarding implementation, he is committed to working together with the Congress to make the reform proposals a reality.

The OIG is a proponent of the eventual merging of the BIF and SAIF. The OIG also believes that when such a merger occurs, the timing is opportune for the OIG to become the auditor of record for the FDIC. A shift of responsibility for the audit of the Corporation's financial

statements from the U.S. General Accounting Office (GAO) to the OIG would be in line with the Chief Financial Officers Act and other agencies' practices. Over the past 5 years, OIG staff members have worked closely with GAO on the financial statement audit effort, assuming increasing responsibility for the work with a goal of assuming full responsibility. The OIG will continue to work to this end. (See later write-up on GAO/OIG Financial Statement Audit Partnership.)

Managing Information Technology

Accomplishing information technology (IT) goals efficiently and effectively requires significant expenditures of funds and wise decision-making and oversight on the part of FDIC managers. The preliminary estimate of the Corporation's 2002 IT budget is \$192.5 million.

IT is increasingly impacting every facet of our lives and is evolving at an ever-increasing pace. The Corporation must constantly evaluate technological advances to ensure that its operations continue to be efficient and cost-effective and that it is properly positioned to carry out its mission of insuring and supervising the nation's financial institutions. The capabilities provided by the IT advances like paperless systems, electronic commerce, electronic banking, and the instantaneous and constant information-sharing through Internet, Intranet, and Extranet sources also pose significant risks to the Corporation and the institutions that it supervises and insures. Many of these risks are new and unique. Therefore, solutions to address them are sometimes difficult and, in many cases, without precedent.

In addition to technological advances, the Corporation must continue to respond to the impact of new laws, regulations, and legal precedents on its activities. Management of IT resources and IT security have been the focus of several significant legislative acts, such as the Government Performance and Results Act and the Paperwork Reduction Act. In addition, pursuant to the Government Information Security Reform Act, the OIG will conduct annual evaluations of the FDIC's information security programs and practices.

While conducting its audit of the Corporation's 2000 and 1999 financial statements, GAO identified a number of general control weaknesses that are rooted in the lack of a fully implemented and effective corporate-wide security program. The Corporation must continue to implement its plans for addressing these weaknesses.

In a related vein, during the reporting period we completed work and issued our final report on our first Independent Evaluation of the FDIC's Information Security Program Required by the Government Information Security Reform Act. This comprehensive report was the most significant product relating to information resources that we issued during the reporting period.

Independent Evaluation of the FDIC's Information Security Program Required by the Government Information Security Reform Act

Recognizing the need to ensure proper management and security of information resources in all federal agencies, on October 30, 2000, President Clinton signed the Floyd D. Spence National Defense Authorization Act for Fiscal Year 2001 that included amendments to Chapter 35 of Title 44, United States Code. This legislation is commonly referred to as the Government Information Security Reform Act (GISRA). The GISRA requires each agency head to submit annually to the Director of the Office of Management and Budget (OMB) the

results of agency and Inspector General evaluations of the agency-wide information security program. We issued a report addressing the requirement for an OIG independent evaluation.

Our review addressed management controls associated with questions posed by the OMB in June 2001 reporting guidance. We primarily relied on OMB Circular A-130, Appendix III, as criteria for the major elements of an effective information security program. For each question, we provided our assessment in terms of level of assurance that the established and implemented controls provide an adequate level of security. We also developed an overall rating of the Corporation's information security program using the individual ratings of each control, taking into consideration their associated risk.

Overall Assessment

We concluded that there is limited assurance that the Corporation has established and implemented an overall information security program that provides adequate security. Delays in completing the key documentation listed below impaired progress toward achieving reasonable assurance of adequate security:

- A corporate-wide security plan,
- Major application and general support systems security plans,
- Authorizations to process,
- An enterprise architecture, and
- An information technology capital plan.

[Graphic in tabular form of FDIC OIG's Assessment of the FDIC's Information Security Program]

[Text Description of table of FDIC OIG's Assessment of the FDIC's Information Security Program- In the Risk Management Control area, the rating for establishment of controls was reasonable assurance. The rating for implementation of controls in this area was limited assurance. In the General Support System and Application Security Control area, the rating for establishment of controls was limited assurance. The rating for implementation of controls in this area was limited assurance. In the Training Control area, the rating for establishment of controls was limited assurance. The rating for implementation of controls in this area was no assurance. In the Incident Response Capability Control area, the rating for establishment of controls was limited assurance. The rating for implementation of controls in this area was limited assurance. In the Capital Planning and Investment Control area, the rating for establishment of controls in this area was limited assurance. The rating for implementation of controls in this area was no assurance. In the Critical Asset Protection Control area, the rating for establishment of controls was limited assurance. The rating for implementation of controls in this area was limited assurance. In the Performance Measurement Control area, the rating for establishment of controls was no assurance. The rating for implementation of controls in this area was no assurance. In the Integration of Security Activities Control area, the rating for establishment of controls was limited assurance. The rating for implementation of controls in this area was limited assurance *. In the Contractor and External Security Control area, there was no rating. There was no rating for implementation of controls in this area as well *.

* Note: we plan to complete our assessment of management control areas related to contractor and external information security policies and practices as part of the next annual cycle of GISRA-related audits and evaluations.]

[The following is a continuation of the major issues section of the semiannual report]

In general, the FDIC had made progress in establishing management controls, including acknowledging the need for key security program documentation, but had not always thoroughly or timely implemented those controls. The Corporation had also been working to address information security issues previously identified in OIG, GAO, and its own internal reviews. The FDIC plans to complete numerous actions to strengthen information security by December 31, 2001. The matrix above summarizes the results of our evaluation.

The Corporation is not reporting any material weaknesses to the OMB as a result of its program reviews of information security required by the GISRA. However, in three of nine key management control areas (training, capital planning and investment control, and performance measurement), the FDIC had no assurance that adequate security had been achieved. These findings are especially significant given the interrelated nature of the components of the overall information security program. If not the focus of prompt management attention, these three areas may warrant reporting as individual material weaknesses in the next Statement on Internal Accounting and Administrative Controls prepared by the FDIC in order to comply with the Chief Financial Officers Act of 1990, as amended, and due by June 30, 2002. The OIG will continue to work with the Corporation to address areas of concern identified through our independent evaluation.

Our work related to information technology management also included issuance of four other reports during the period.

The FDIC's ISR Process

We completed an audit of the FDIC's independent security review (ISR) process. We performed the audit at the Division of Information Resources Management's (DIRM) request to comment on process-related improvement opportunities identified during our earlier work on the ISR of the FDIC's mainframe computer system. The objective of our report and our limited audit procedures was to identify and develop process-related observations and suggestions for improving the ISR program.

We identified several improvement opportunities to enhance the ISR program so that it can better serve as an effective management tool for detecting security weaknesses. Because of the consultative nature of the assignment we made suggestions rather than formal recommendations. DIRM is reassessing its ISR approach and has begun to revise the ISR procedures manual, the ISR format, and the ISR process to incorporate our suggested improvements.

The FDIC's Chief Information Officer and DIRM Director's response to our report agreed with all but one suggestion. DIRM believes that increasing the number of ISRs through component analysis for general support systems is counterproductive and will not substantially add to the "likelihood of learning useful information to improve security" as

defined in OMB A-130, Appendix III. In our view, breaking general support systems into components for review allows DIRM to better focus on significant risks in those systems. Accordingly, we suggested that DIRM reconsider its decision as the ISR process matures.

Receivership Liability System Security and Data Validation

We concluded that the FDIC established a good security structure for the Receivership Liability System (RLS). Specifically, DIRM developed RLS with two layers of access security. Also, the Division of Resolutions and Receiverships conducted reviews of initial access requests and semiannual security reviews of the national system to limit access to sensitive data. We did find, however, that better security reviews and additional security-related procedures would enhance system security. Good procedures were also in place for transferring data from former systems to RLS. Data encryption technology had been added to help ensure that information transmitted from bank closings was secure, and management was able to review user activity. However, we determined that the chances for inaccurate or incomplete data loads could be further reduced by improving reconciliation procedures, verifying record count totals transmitted from bank closings to the national database, strengthening the data certification process, and improving storage of archived RLS audit tables. We made 13 recommendations to address these concerns and management agreed to take action on all of them.

The FDIC's Planning for the Institution Data Management Project

We completed our audit of the Corporation's Institution Data Management (IDM) project. This project is a corporate-wide initiative to improve the collection, processing, storage, and dissemination of open financial institution data. Our audit objective was to monitor the progress of the IDM project and provide input at critical milestones or when conditions warranted. As part of the audit we evaluated whether the IDM project team was adequately coordinating with related application development projects and information technology initiatives.

The IDM project presents the FDIC with opportunities to improve the manner in which it collects, processes, stores, and disseminates open institution data. However, progress on the project has not met expectations. Our report contained two recommendations designed to improve progress on the project. The first was intended to build consensus among the IDM project stakeholders regarding key aspects of the project, such as the project's goals and objectives, scope, requirements, and timeframes. The second recommendation was designed to ensure that senior FDIC management is continually apprised of the project's status. These recommendations were intended to promote a corporate approach to the IDM concept and keep the project's scope, requirements, and progress on target.

We also suggested that the IDM project team will need to closely coordinate its work with related information technology projects and business process studies as the project moves forward so that resources are not duplicated or unnecessarily expended. We recommended that, as part of building consensus among stakeholders, FDIC management ensure that such coordination takes place.

The Chief Operating Officer and Chief Financial Officer provided a joint response to the draft audit report that satisfied the concerns we raised.

The FDIC's Development of Its Public Key Infrastructure

We issued the results of our audit of the FDIC's development of its Public Key Infrastructure (PKI). A PKI is a system of hardware, software, policies, and people that, when fully and properly implemented, can provide a suite of information security assurances that are important in protecting sensitive communications and transactions. The FDIC initiated the development of a PKI in 1996. Since 1997 our office has been providing the FDIC with suggestions and recommendations for improving its PKI development process. We estimated that the FDIC expended over \$3 million through calendar year 2000 in an effort to effectively implement a PKI that benefits the Corporation.

Our report provided DIRM with additional recommendations to improve the PKI development process. We recommended that DIRM develop PKI documents using National Institute of Standards and Technology standards and GAO guidelines and adhere to established milestones for the PKI development effort. In addition, the FDIC should develop an e-government implementation plan using OMB's guidelines for implementing the Government Paperwork Elimination Act. The Corporation agreed with our recommendations.

Ensuring Sound Controls and Oversight of Contracting Activities

The private sector provides goods and services to the Corporation as needed through contracting to assist the FDIC in accomplishing its mission. Contractors assist the FDIC in many areas including information technology, legal matters, property management, loan servicing, asset management, and financial services.

Maintaining a strong system of internal controls and effective oversight of contracting activities is critical to the FDIC's success. The Corporation has taken a number of steps in this regard—training, revisions to the Acquisition Policy Manual, its Contractor Oversight Summit. It has added a goal regarding contractor oversight to its Annual Performance Plan, which is formulated in accordance with the Government Performance and Results Act. It must work to sustain these efforts going forward.

Projections of year 2002 non-legal contract awards and purchases total

1,800 actions valued at approximately \$380 million. One of the most active areas of contracting in the Corporation regards information technology. As of September 30, 2001, there were more than 230 active information resources management contracts valued at approximately \$350 million that had been awarded in headquarters. Approximately \$150 million of this expenditure authority for active contracts had been spent and

\$200 million remained to be used as of that time.

We issued two reports involving FDIC contracting activities during the reporting period, including the following.

Training and Consulting Services Branch Contracts Over \$100,000

We concluded that the contracts reviewed (6 out of 13 contracts over \$100,000) met the needs of customers. However, the FDIC can take initiatives to improve the timeliness and tracking of Training and Consulting Services Branch (TCSB) contracts over \$100,000. In addition, the

Acquisition and Corporate Services Branch personnel were not consistently following procedures for entering completion dates into the Procurement Action Log related to the tracking of significant contracting phases for the six contracts. As a result, the usefulness of the Procurement Action Log information was reduced. We made four recommendations to address these issues, with which management agreed.

As part of our audit we met with officials from other government agencies to identify contracting practices and training services that the FDIC could consider to further improve the timeliness and delivery of training services to customers. As a result, we identified two suggestions related to TCSB using a basic ordering agreement to award contracts and the Department of Transportation's Transportation Virtual University program to expand training options. DOA was exploring use of a basic ordering agreement during our audit.

Other Contracting Activity

During the reporting period, the OIG also took part in the Office of Internal Control Management's (OICM) Contractor Summit meeting to discuss contractor oversight issues with FDIC divisions and offices. Additionally, we participated in "workout" teams with other divisions and offices. These teams provide possible solutions to oversight problems concerning contract scope and modifications, contractor qualifications and labor mix, and invoice submission and review. These are areas that the OIG has shown to be problematic. Our involvement allowed us to provide advice on a proactive basis before final decisions were made. The OIG also participated in another OICM-sponsored initiative to evaluate project management courses that could be included in the Corporation's oversight manager curriculum.

Ongoing work in the contracting area includes several billing and performance reviews of contractors providing IT-related services to the Corporation.

Establishing Goals and Measuring Results

The Government Performance and Results Act (Results Act) of 1993 was enacted to improve the efficiency, effectiveness, and accountability of federal programs by establishing a system for setting goals, measuring performance, and reporting on accomplishments. Specifically, the Results Act requires most federal agencies, including the FDIC, to prepare a strategic plan that broadly defines the agencies' mission, vision, and strategic goals and objectives; an annual performance plan that translates the vision and goals of the strategic plan into measurable annual goals; and an annual performance report that compares actual results against planned goals.

The Corporation's strategic plan and annual performance plan lay out the agency's mission and vision and articulate goals and objectives for the FDIC's three major program areas of Insurance, Supervision, and Receivership Management. The plans focus on four strategic goals that define desired outcomes identified for each program area. These four goals are: (1) Insured Depositors Are Protected from Loss Without Recourse to Taxpayer Funding, (2) FDIC-Supervised Institutions Are Safe and Sound, (3) Consumers' Rights Are Protected and FDIC-Supervised Institutions Invest in Their Communities, and (4) Recovery to Creditors of Receiverships Is Achieved. Through its annual performance reports, the FDIC is accountable for reporting actual performance and achieving these strategic goals, which are closely linked to the major issues discussed in this semiannual report.

The Corporation has made significant progress in implementing the Results Act and will continue to address the challenges of developing more outcome-oriented performance measures, linking performance goals and budgetary resources, establishing processes to verify and validate reported performance data, and addressing crosscutting issues and programs that affect other federal financial institution regulatory agencies. The FDIC is committed to fulfilling both the requirements of the Results Act and congressional expectations that the performance plans and reports clearly inform the Congress and the public of the results and outcomes of the FDIC's major programs and activities, including how the agency will accomplish its goals and measure the results.

OIG Formulates Results Act Review Plan

In late 1998, the House Leadership formally requested that the Inspectors General of 24 executive agencies develop and implement a plan for reviewing their agencies' Results Act activities. The Results Act review plan would be included and updated annually as part of the OIG's semiannual reports to the Congress and would examine (1) agency efforts to develop and use performance measures for determining progress toward achieving performance goals and program outcomes described in their annual performance plan and (2) verification and validation of selected data sources and information collection and accounting systems that support Results Act plans and reports. Findings and recommendations from Results Act reviews would be included in each subsequent semiannual report. The Congress attaches great importance to effective implementation of the Results Act and believes that Inspectors General have an important role to play in informing agency heads and the Congress on a wide range of issues concerning efforts to implement the Results Act. We believe the congressional guidance represents an appropriate direction for all Offices of Inspector General.

OIG's Results Act Review Plan

The FDIC OIG is fully committed to taking an active role in the Corporation's implementation of the Results Act. We have developed a review plan to help ensure that the Corporation satisfies the requirements of the Results Act and maintains systems to reliably measure progress toward achieving its strategic and annual performance goals. Our review plan consists of the following three integrated strategies:

- **Linking Planned Reviews to the Results Act.** We will link planned reviews to corporate strategic goals and annual performance goals and provide appropriate Results Act coverage through audits and evaluations. As part of this strategy, one of the goals of our planning effort this year is to align our audit work more closely with the Corporation's strategic plan and performance goals.
- **Targeted Verification Reviews.** We will maintain a program of independent reviews to evaluate the adequacy and reliability of selected information systems and data supporting FDIC performance reports. The OIG has developed a standard work program to conduct these evaluations.
- **Advisory Comments.** We will continue our practice of providing advisory comments to the Corporation regarding their update or cyclical preparation of strategic and annual performance plans and reports.

OIG Provides Results of Analysis of FDIC 2000 Performance Measures to Chairman Burton

During the reporting period we provided Congressman Dan Burton, Chairman of the House Committee on Government Reform, with the results of our analysis of the FDIC's 2000 performance measures. Chairman Burton had requested that the Inspectors General of 24 major federal departments and independent agencies provide an assessment of what they consider to be the ten most significant performance measures contained in their agency's performance reports issued under the Results Act. He also requested they indicate the extent to which the data or information underlying the measures is valid and accurate. The FDIC was not one of the 24 agencies specifically included in Chairman Burton's request; however, we support his interest in the validity and reliability of performance measures. Accordingly, we analyzed the FDIC's performance measures in the same general framework as requested in his letter to the Inspectors General.

Based on our analysis and after coordination with the Division of Finance, we identified ten performance measures in the draft FDIC 2000 Program Performance Report as being the most significant. Our list included performance measures for each of the Corporation's four direct mission strategic result areas as follows: four measures related to protection for insured depositors; three measures related to safety and soundness of depository institutions; one measure related to protection of consumer rights and community investment; and two measures related to receivership management and recovery to creditors. Our response noted that while the ten measures are not perfect outcome-oriented performance measures, we believe the measures represent useful, valid measures that are relevant to critical FDIC mission areas. We also noted that the OIG has performed verification and validation review work related to nine of the ten measures. Documentation of verification and validation procedures was satisfactory for five of the nine performance measures reviewed. For the other four measures, documentation was adequate to support reported data (for the period under review); however, the FDIC could better document verification and validation procedures performed. The FDIC is taking OIG-recommended action to improve procedures.

In a related matter, we provided FDIC management with our summary views of the most important corporate and OIG performance measures for assessing performance in 2002. The information was provided in response to a request from Chairman Powell's Task Force on Measuring Corporate Performance. Our views of corporate measures were built on our previous analyses, particularly our analysis for Congressman Burton of the Corporation's ten most important performance measures. As we have mentioned in various advisory memoranda to management and in our Semiannual Reports to the Congress, we believe the identification of high quality performance measures is one of the Corporation's major management challenges. We look forward to continuing to work with the Corporation, through our various reviews and analyses, to help meet this challenge.

OIG Reviews FDIC 2001 - 2006 Strategic Plan

During this reporting period, the OIG also reviewed and provided advisory comments to management on the FDIC's draft 2001 - 2006 Strategic Plan. We noted that positive changes have been made in streamlining the strategic plan both in structure and in length. We also offered some observations and suggestions to FDIC management for improving the plan in several areas.

- *Perspective on the FDIC Supervisory Role* – provide additional perspective on the FDIC supervisory role—to include the number and size of FDIC-insured institutions supervised by the FDIC in relation to those supervised by the other banking regulatory agencies and the

potential impact of this regulatory relationship;

- *External Factors* – reevaluate the external factors included for each strategic objective to consider whether additional factors should be added, particularly factors related to economic downturn, changes in the structure of the financial system (mergers and consolidation, financial globalization, and legislation), and risks identified in OIG reports;
- *Interagency Crosscutting Issues* – present a brief discussion of the most significant interagency crosscutting issues that are being addressed or should be addressed during the period covered by the plan;
- *Supervision and Receivership Management Strategic Initiatives* – include a concise description of the supervision and receivership management strategic initiatives that will be emphasized;
- *Human Capital Strategic Initiatives* – provide a more complete discussion of the FDIC’s critical human capital strategic initiatives;
- *Quality and Outcome Orientation of Performance Measures* – include a reference to the FDIC’s commitment to continue to improve the quality and outcome orientation of performance measures; and
- *OIG Strategic Plan* – include a reference to the OIG Strategic Plan.

Management incorporated changes related to our suggestions for all of the areas, except for External Factors and Interagency Crosscutting Issues, into the final version of the plan.

The OIG will continue to develop and refine its integrated oversight strategy to help ensure that the FDIC’s Results Act-related efforts fully conform to the spirit and intent of the Act. We plan to continue to work with the Corporation to improve the FDIC’s performance measurement and reporting through our audits, evaluations, and management advisory reviews and analyses. The OIG will also continue to monitor and review legislation proposed in the Congress to amend the Results Act and will actively participate to refine appropriate OIG Results Act roles, responsibilities, and activities through the President’s Council on Integrity and Efficiency and the interagency groups it sponsors.

Addressing Human Capital Issues

Since 1994, as the work emanating from the banking and thrift crises has declined and continued consolidation of the financial services industry has occurred, the FDIC has accordingly reduced its workforce substantially. The workforce has fallen from a high of about 15,600 in mid-1992 to 6,326 as of September 22, 2001. In addition to reductions in the size of the workforce, as the Corporation’s needs have changed, employees have been relocated to best serve those changing needs.

The FDIC has faced staffing shortages in certain critical skill areas owing to the loss of such a high number of staff and strict prohibitions on hiring from 1992 through 1997. Additionally, through the use of employee buyouts, early retirements, and other downsizing activities, the Corporation has lost a number of highly experienced managers and senior technical experts. Currently, two key positions within the Corporation’s management structure are vacant: the

Director of the Division of Supervision and the position of Chief Information Officer/Director, DIRM.

The Corporation predicts that approximately one of every six remaining FDIC employees will be eligible to retire by year-end 2003. The Corporation must continue to conserve and replenish the institutional knowledge and expertise that has guided the organization over the past years. Hiring and retaining new "federal" talent will be extremely important, particularly given the competitive job market and the lure for many to work in the private sector. Hiring and retention policies that are fair and inclusive remain a significant component of the corporate diversity plan.

Another consideration will be determining where corporate employees will be housed over the long-term. Millions of dollars are spent on leases throughout the country. Given the changes in the industry, such trends as telecommuting and increased use of technological tools to perform work, and continued attrition, the Corporation may need to relocate or establish new work sites and capabilities for its staff over time. During the reporting period, the OIG conducted two reviews relating to the Corporation's work locations. One addressed field office sites and the other focused on options for housing headquarters employees. (See write-ups in next section.)

To implement a successful human capital framework, organizations need information systems that allow managers to identify skills imbalances and project future needs. Also of importance is that the Corporation's human capital strategy and workforce planning system are directly linked to the FDIC's overall strategic and performance plans. The Corporation's 2001-2006 strategic plan includes workforce issues and a discussion of corporate resources. Additionally, the Corporation has worked with a contractor to develop a human capital strategy. Designing, implementing, and maintaining effective human capital strategies are critical to improving performance and accountability and must be the focus of sustained attention.

Containing Costs and Assessing Business Processes

This year has been an important year for identifying and implementing ways to contain and reduce costs, either through more careful spending or assessing and making changes in business processes to increase efficiency.

Following several years of downsizing the Corporation is focusing earnestly on the efficiency of its business processes. The banking industry is placing increased scrutiny on the operating expenses of the Corporation. In addition, the FDIC may no longer be able to count on sizeable savings from office closings to offset the large projected increases in personnel compensation costs.

The Corporation is taking steps to increase emphasis in this area. Several initiatives are in progress to better understand what the various business processes and activities within the FDIC cost, how they can be made more efficient, and how they compare to private and public sector entities. The Corporation may also need to recognize and plan for unmet needs or needs that may not have been sufficiently met, all of which can add to operating costs. Such needs may include, for example, ensuring information resources security and building security.

FDIC Chairman Powell recently underscored the importance of the efficiency and effectiveness of the FDIC in a September 24, 2001 global message to all FDIC employees:

"Because we don't know what challenges the future holds, it has never been more important for us to do the best job we can do, and in the most effective and efficient ways that we can...With that in mind, I have asked a number of colleagues to think—on a corporate, not just a divisional, level—about whether and how our internal operations can be made more effective and efficient. They are beginning their assessment immediately and will be providing me with some ideas over the next couple of months."

Over the past months, the OIG has been called upon to provide FDIC senior management information regarding a number of its business process activities and initiatives for containing costs. During the reporting period we issued the results of evaluation reviews in four key areas. We coordinated with OICM in conducting the third review discussed below:

Field Office Cost, Space Utilization, Design, and Usage

The FDIC will need to make a number of decisions regarding the Corporation's field office structure, location, and corresponding costs. We performed an evaluation to gather information for management's consideration and use when making such decisions. Our objectives were to evaluate:

- Non-personnel costs of FDIC field offices,
- Field office space utilization, design, and usage,
- The impact of telework on field office decisions, and
- FDIC field office facilities against other benchmark entities.

We reported the following to management:

Annual Field Office Costs

FDIC field offices cost roughly

\$17.5 million annually. Leasing costs and information technology costs accounted for the bulk of total FDIC field office costs, respectively. We benchmarked selected costs against the Office of the Comptroller of the Currency and communicated our observations.

Field Office Space Utilization

The FDIC's ratio of rentable square feet to field office employees, known as the utilization rate (UR), was higher than the URs of other government benchmarks that we reviewed.

Further, the amount of the FDIC's field office space increased markedly over the past few years. Specifically, the FDIC's median UR increased by 146 percent under its current set of field office leases. FDIC officials indicated one reason for this increase was because the amount of field office space was probably not sufficient under prior leases, but acknowledged the FDIC may have overcompensated in improving and expanding field office space.

Field Office Space Design

In March 1999, the FDIC agreed to provide dedicated cubicles to all field examiners, an initiative called 1:1. The space required to implement 1:1 accounted for about 28 percent of the increase in leased space under the FDIC's current set of leases. Other design features, such as training rooms, conference rooms, storage, and DIRM space accounted for the balance of the increase. The Division of Administration updated the FDIC Facilities Design Guide following our review and now encourages field offices to combine training and conference room space.

Field Office Usage Levels

During 2000, field examiners spent a median of about 33 percent of their time in FDIC field offices. DOS and Division of Compliance and Consumer Affairs (DCA) examiners spent 32 and 35 percent of their time in field offices, respectively. We understand that in conjunction with the telework program, FDIC will begin monitoring field office usage to determine future facilities needs.

Telework

In May 2001, the FDIC offered task-based telework to all employees and home-based telework to a limited number of DCA field examiners.

DOS officials mentioned the team approach to conducting examinations as the greatest challenge to teleworking. DCA officials indicated their examination approach would be more suited to teleworking because many of DCA's examination teams consist of one or two members.

We researched case studies at other agencies and private sector companies to determine what characteristics of telework programs enabled reductions in facilities space. Although our research was not fully conclusive, a common characteristic of such telework programs was that teleworkers did not have dedicated cubicles or offices.

Subsequent to our review we learned that in addition to the change in the FDIC Facilities Design Guide referenced above, management also removed certain information technology requirements from the guide. Instead of applying the requirements on a blanket basis, they will be addressed case-by-case.

Review of the FDIC's Long-Term Headquarters Housing Study

We issued a report to FDIC Director Reich communicating the results of our evaluation of the reasonableness of the FDIC's Long-Term Headquarters Housing Study (Study) updated by Spaulding and Slye Colliers (S&S) in December 2000. The purpose of the Study was to identify and evaluate office space options and to recommend the most cost-efficient long-term strategy to house FDIC headquarters employees.

The Study presented comparative net present value (NPV)¹ cost information for eight housing options suggested for review by the FDIC's Acquisition and Corporate Services Branch. We limited our evaluation to cost items and assumptions supporting S&S' December 21, 2000 Study and subsequent corrections to the Study. We focused our review on the three scenarios that the FDIC would most likely pursue: (1) Renew existing leases at the 801 17th Street, 1717 H Street, and 1700 and 1730 Pennsylvania Avenue buildings (Status Quo), (2) Lease

new space in Virginia (VA Lease), and (3) Develop a second facility at Virginia Square (Phase II).

We concluded that the study assumptions, space requirements determination, market survey, and analysis methodology were reasonable, complete, and supportable. Further, we concluded that Phase II remains the least cost alternative of the options considered. After adjusting the Study for certain items discussed in our report, the 20-year NPV cost of the Phase II option is \$89.9 million less than the Status Quo option and

\$48.6 million less than the VA Lease option.

We also concluded that S&S used an acceptable private sector approach in analyzing and valuing each housing option. However, we identified several calculation errors, two of which significantly altered the NPV cost of the three housing options that we reviewed. S&S issued a revised financial analysis in August 2001 that corrected most of the calculation errors.

We also addressed several other issues related to the Study that management should consider in determining its long-term strategy to house FDIC headquarters employees.

OIG and OICM Issue Final Report on the FDIC's Corporate Planning Cycle

The OIG Office of Corporate Evaluations and OICM completed their study of the FDIC's Corporate Planning Cycle (CPC) that was requested by the Chief Financial Officer. As a complement to the Division of Finance's review of the Strategic Planning, Core Staffing, Budget Formulation, and Budget Execution processes, the purpose of the study was to determine the extent of resources involved in carrying out and supporting the CPC and to identify areas where there may be opportunities to more effectively integrate and streamline these processes.

Based on the information provided, we identified 560 individuals, excluding senior corporate executives, 29 Division of Finance staff and the 16 division and office directors, including the Inspector General, who participated in the CPC during the 2001 cycle. Ninety-five percent of those involved participated in the process as a collateral duty. We also identified seven contracts used since 1998 related to CPC. Of the approximately \$3.2 million expended in that time, over 50 percent related to system development and maintenance costs for the Business Planning System and Budget Manual Update, and over 35 percent related to the Division of Resolutions and Receiverships' service costing initiative.

We also made the following observations that are intended to complement the Division of Finance's review:

- Consider converting to a 2-year budget cycle to reduce the level of effort required each year;
- Evaluate further the timing and integration of the planning, staffing, and budgeting components of the process after the 2002 CPC;
- Ensure that annual division and office performance plans become more useful and better linked to the corporate plan;
- Integrate better the procurement and information technology plans into the process; and

- Improve communication of initiatives and the Division of Finance's role in the process.

Study of Internal Control and Internal Review Programs

At the request of the Chief Financial Officer, the Office of Corporate Evaluations performed a study to identify the resources devoted to internal control and internal review programs and determine whether any potential exists for streamlining these programs. We focused on two major segments of the Corporation: OICM (an independent office reporting to the Deputy to the Chairman and Chief Financial Officer) and eight divisions and offices that have internal review organizations reporting to their divisions' management.² The resources currently devoted to internal review include:

[Footnotes]

1-The NPV is the current value of a project determined by applying an appropriate discount rate to the cash outflows and inflows over the period of analysis. In the FDIC's case, the discount rate is based on Treasury securities.

2-The divisions and offices with internal review organizations include: the Division of Finance, Division of Resolutions and Receiverships, Office of Inspector General, Division of Administration, Division of Information Resources Management, Division of Compliance and Consumer Affairs, Division of Supervision, and the Legal Division.

- 91 full-time OICM and internal review organization staff at an annual cost of \$11.5 million (based on 2001 average salary and benefits by grade);
- 97 collateral Internal Control Liaisons (ICL), back-up ICLs, and Accountability Unit Managers; and
- 90 assistants who helped conduct reviews in 107 instances during 2000.³

Although we did not assess the FDIC's internal control program nor review the effectiveness of OICM and the eight internal review organizations, our results indicate that going forward the Corporation should consider a number of steps in evaluating its internal control and internal review efforts.

Specifically, the Corporation would be well served to first determine more definitively the time and resource levels currently devoted to these activities, paying close attention to time and resources various groups are spending strictly on risk management functions versus other/competing tasks. In so doing the Corporation could also identify areas of potential overlap of coverage. Second, consideration should be given to the actual results of the various internal control and internal review efforts, looking at which risk areas have been reduced, the overall results of the accountability unit risk rating process, and the results of other more routine internal review activities such as time and attendance reviews.

In light of that knowledge, the Corporation would be better positioned to make informed decisions on the level of resources that should be devoted to the risk management area and how these resources should be aligned organizationally—given current and anticipated risks for the FDIC, relative to total individual division and office staffing, and as a function of a division or office being considered a "driver" division of the Corporation.

In late September the Corporation announced that OICM would initiate a study to (1) determine the actual number of staff performing purely internal control-related functions; (2) determine the number, types, and frequency of internal-control related products that are produced; and (3) provide organizational options for streamlining the internal control activities of FDIC divisions and offices.

[Footnote]

3 - These 90 employees do not perform reviews full-time and may participate in more than one review during a year.

[Contained in the Major Issues section of the report is a panel titled - "OIG's Initiative in Financial Statement Auditing Continues to Advance"]

[Start of OIG's Initiative in Financial Statement Auditing Continues to Advance panel]

OIG's Initiative in Financial Statement Auditing Continues to Advance

The FDIC OIG and U.S. General Accounting Office (GAO) have conducted the financial statement audits of the FDIC funds for the past several years. Working side by side with GAO has enabled the OIG to enhance its proficiency in financial statement auditing. This initiative has also afforded the OIG the unique opportunity to combine both financial auditing and performance auditing disciplines. Additionally, the GAO/OIG has developed a fuller understanding of the FDIC's financial management operations and emerging financial management issues facing the Corporation. The OIG will capitalize on this foundation going forward.

During this reporting period the OIG reorganized the financial statement auditing team into the Financial Management Directorate. For the remainder of 2001, some of the Directorate team members will continue to work with GAO in conducting the financial statement audits, while other team members will review financial management performance aspects of the Corporation. In addition, the OIG is working to assume full responsibility for the financial statement audits in 2002.

Aside from the financial statement audit work, current projects in the financial management area include audits of the capitalization of software development costs, the FDIC's strategies for managing improper payments, the accounts payable purchase order vendor file, and the asset valuation review process.

[End of panel on OIG's Initiative in Financial Statement Auditing Continues to Advance]

[The Following is a continuation of the Major Issues section of the Semiannual Report]

OIG Work Addresses Emerging Physical and Personnel Security Issues

OIG Will Evaluate Physical Security of FDIC Facilities

The OIG is beginning an evaluation of the adequacy of physical security of FDIC facilities. We will place particular emphasis on the security measures taken to provide a safe work environment for FDIC employees and visitors. We will also determine whether the FDIC's

safety and environmental management policies for real property have been established and implemented to:

- protect Federal real and personal property,
- promote mission continuity,
- assess risk,
- make decision makers aware of risks, and
- act promptly and appropriately in response to risk.

We will perform field work at FDIC facilities located in major cities as well as other selected sites throughout the country.

OIG Reviews the FDIC's Background Investigation Process for Prospective and Current Employees; Management Responds Promptly

The OIG conducted a review of the FDIC's background investigation process based on a request from the Subcommittee on Oversight and Investigations, Committee on Financial Services, U.S. House of Representatives. The Subcommittee Chairwoman, Sue W. Kelly, requested that we evaluate the FDIC's policies, procedures, and practices under which the Corporation conducts, adjudicates, and documents background investigations of prospective and current employees. Additionally, at the Corporation's request, we assessed whether the Corporation had effectively implemented a process to ensure that proper risk designations had been assigned to the FDIC's positions.

We found that the FDIC needs to do more to ensure that all corporate positions have risk designations and that such designations are commensurate with assigned responsibilities and reflected accurately in corporate databases. Most significantly, the FDIC assigned a low-risk designation to nearly all of its safety and soundness and compliance examiners. In addition, the FDIC did not always consider automated data processing implications for positions outside of its information resources management division.

The Corporation's policies and procedures regarding employee background investigations comply with provisions of applicable federal laws and regulations. In addition, the FDIC generally conducted, adjudicated, and documented the investigations for current and prospective employees in accordance with corporate policies and procedures.

We made eight recommendations to address the issues in our report, and the Corporation tentatively agreed with them. Because the recommendations involved a number of divisions and offices, the Corporation needed additional time to provide a formal response. We informed Chairwoman Kelly that we would provide her information on the response when we received it. The Corporation issued a memorandum to the OIG several weeks later outlining the actions that the Corporation has already taken or is planning to take as a result of our review.

As indicated in its response, the Corporation's security and personnel branches had already met to discuss initiatives for reconciling risk designation differences in their respective

databases and communicating risk designation changes as they take place. The Corporation agreed to raise the Low-Risk designation of its examiner positions to Moderate-Risk, and the FDIC established a timeframe to complete appropriate background investigations on current bank examiners requiring more extensive investigations as a result of risk-level changes. The Corporation also determined that its Information Security Manager positions will be designated High-Risk Public Trust positions, and the FDIC will conduct background investigations of its employees working in these positions, as appropriate.

[End of Major Issues section of the Semiannual Report]

[Start of the Investigations Section of the Semiannual report]

Investigations

The Office of Investigations (OI) is responsible for carrying out the investigative mission of the OIG. Staffed with agents in Washington, D.C.; Atlanta; Dallas; and Chicago; OI conducts investigations of alleged criminal or otherwise prohibited activities impacting the FDIC and its programs. As is the case with most OIG offices, OI agents exercise full law enforcement powers as special deputy marshals under a blanket deputation agreement with the Department of Justice. OI's main focus is in investigating criminal activity that may harm or threaten to harm the operations or the integrity of the FDIC and its programs. In pursuing these cases, our goal, in part, is to bring to a halt the fraudulent conduct under investigation, protect the FDIC and other victims from further harm, and assist the FDIC in recovery of its losses. Another consideration in dedicating resources to these cases is the need to pursue appropriate criminal penalties not only to punish the offender but to deter others from participating in similar crimes.

Joint Efforts

The OIG works closely with U.S. Attorneys Offices throughout the country in attempting to bring to justice individuals who have defrauded the FDIC. The prosecutive skills and outstanding direction provided by the Assistant United States Attorneys with whom we work are critical to our success. The results we are reporting for the last 6 months reflect the efforts of U.S. Attorneys Offices in the Middle District of Florida, Southern District of Florida, Southern District of Illinois, District of Maryland, District of Massachusetts, District of Hawaii, Eastern District of Pennsylvania, Northern District of Mississippi, District of Arizona, Eastern District of Virginia, and Southern District of West Virginia.

Support and cooperation among other law enforcement agencies is also a key ingredient for success in the investigative community. We frequently "partner" with the Federal Bureau of Investigation (FBI), the Internal Revenue Service (IRS), Secret Service, and other law enforcement agencies in conducting investigations of joint interest.

Results

Over the last 6 months OI opened 15 new cases and closed 21 cases, leaving 117 cases underway at the end of the period. Our work during the period led to indictments or criminal charges against 18 individuals or entities. Ten defendants were convicted during the period. Criminal charges remained pending against 13 individuals as of the end of the reporting period. Fines, restitution and recoveries stemming from our cases totaled over \$11.8 million.

The following are highlights of some of the results from our investigative activity over the last 6 months:

Fraud Arising at or Impacting Financial Institutions

Four More Defendants Enter Guilty Pleas in Connection with Ongoing Bank Fraud Investigation Involving the First National Bank of Keystone

Four former officials of the First National Bank of Keystone (Keystone), Keystone, West Virginia, who were charged on April 10, 2001, in connection with alleged illegal activities all subsequently pleaded guilty pursuant to negotiated plea agreements.

On May 21, 2001 the former Vice President and Cashier of Keystone entered a plea of guilty to a one-count Bill of Information charging her with insider trading. The charge resulted from her sale of approximately \$440,000 in Keystone stock about 2 months before the bank was declared insolvent and closed by the Office of the Comptroller of the Currency (OCC).

On June 4, 2001, the former Vice President and Head Bookkeeper, and the former Vice President and Proof Operator of Keystone both entered pleas of guilty to one-count Bills of Information charging them with obstruction of an examination of a financial institution. The charges arose from their roles in the July 1999 examination of Keystone by the OCC and FDIC.

On July 16, 2001, the former Vice President of Keystone Mortgage Corporation, a subsidiary of Keystone, entered a plea of guilty to a two-count Bill of Information charging her with filing false income tax returns. The charges arose from her failure to claim income in the form of "Bonus" payments received from Keystone. She failed to claim \$82,000 in 1996 and \$140,670 in 1997.

Sentencing for all four defendants is scheduled after the end of the current reporting period.

As previously reported, charges of bank embezzlement, conspiracy to commit bank embezzlement, and mail fraud are also pending against the former bank Chairperson of Keystone and the bank's former Senior Executive Vice President and Chief Operating Officer, both of whom were indicted on March 22, 2001. Money laundering charges are also pending against the former bank Chairperson.

The former bank Chairperson and the former Executive Vice President of the mortgage company were convicted and sentenced last year on charges of obstructing an examination of the bank and both are currently in prison serving sentences in excess of 4 years. Following his sentencing in the obstruction case in July, the Executive Vice President of the mortgage company pleaded guilty last November to charges of conspiracy, money laundering, and bank fraud. He is currently awaiting sentencing on those charges. An examination that was conducted by the OCC in 1999 uncovered information that ultimately resulted in the closure of Keystone on September 1, 1999. As the receiver of the bank's assets, the FDIC has thus far reported losses to the insurance fund attributable to Keystone that make it one of the ten costliest bank failures since 1933.

The investigation and prosecutions involving Keystone are being conducted by a multi-agency task force comprised of Special Agents of the FDIC OIG, FBI, and IRS and prosecutors from

the United States Attorney's Office for the Southern District of West Virginia and the U.S. Department of Justice. The FDIC Division of Resolutions and Receiverships has also provided valuable assistance in support of the task force investigations.

Additional Results Obtained from Investigations Involving Former Officers and Customers of Murphy-Wall State Bank

On May 25, 2001, a federal grand jury in the Southern District of Illinois returned an eight-count indictment charging the former president of Murphy-Wall State Bank (MWSB), Pinckneyville, Illinois, with obstructing an examination of the bank, making a false statement to the FBI, making false bank entries, and misapplying bank funds.

As alleged in the indictment, the former president was aware that a company had provided the bank false information regarding the value of collateral offered as security for a \$500,000 loan and had subsequently misapplied the loan proceeds. Allegedly the former president withheld this information from FDIC examiners on two occasions and lied to FBI agents during the investigation about when he became aware of the customer misrepresentations. The former president is also charged in the indictment with five specific instances of making or causing to be made false entries, reports, and statements including material omissions in the books of MWSB, all of which relate to the same customer. The charge pertaining to misapplication of bank funds is based on the former president's alleged knowledge that some of the same loan proceeds would be diverted to pay off two personal loans of individuals connected with a sister company of the borrower.

On June 6, 2001, a former customer of MWSB was sentenced in Federal District Court, Southern District of Illinois, to 4 months in jail, to be followed by 4 months of home detention. Additionally, he was ordered to serve 5 years' probation, fined \$200, and ordered to make restitution of \$157,312 to MWSB.

[Contained in the Investigations section of the report is a panel titled - "Investigative Statistics, April 1, 2001 - September 30, 2001"]

[Start of Investigative Statistics, April 1, 2001 - September 30, 2001 panel]

Investigative Statistics, April 1, 2001 - September 30, 2001

Judicial Actions: There were 18 Indictments/Informations. There were 10 convictions. OIG Investigations Resulted in: Fines of \$ 118,700, Restitution of 9,319,940, Forfeitures Based on Asset Seizures 2,369,908 for a total of \$11,808,548. Ten cases were referred to the Department of Justice (U.S. Attorney). There were 3 referrals to FDIC Management. There were 58 OIG Cases Conducted Jointly with Other Agencies.

[End of Investigative Statistics, April 1, 2001 - September 30, 2001 panel]

[Contained in the Investigations section of the report is a panel titled - "Office of Investigations Responds to Requests for Assistance in Terrorist Investigations"]

[Start of Office of Investigations Responds to Requests for Assistance in Terrorist

Investigations panel]

Office of Investigations Responds to Requests for Assistance in Terrorist Investigations

In the aftermath of the terrorist events of September 11, we are proud of the efforts of our investigative staff.

Beginning September 22nd and running through September 27th when the mission was completed, a group of one to five Office of Investigations (OI) Special Agents per day worked 12-hour shifts on the Evidence Recovery Team at the Pentagon. Seven OI Special Agents volunteered for duty on the Evidence Recovery Team in response to a request by the Federal Bureau of Investigation (FBI) and the Department of Defense for assistance.

At the FBI's request, the OIG community provided investigative support in New York City. Two agents from FDIC OIG volunteered for this assignment which was anticipated to include interviewing, analysis, evidence recovery, and security. The two agents began their detail in New York on September 30.

The FBI's Financial Crimes Section also asked the Inspector General community for special assistance in investigating the funding used to perpetrate the recent acts of terrorism and links to possible future acts. The FBI asked the FDIC OIG's OI to check its records and agency databases for information on the terrorists or suspects. At the time of the request, the FBI list contained over 300 names. Working with the Division of Resolutions and Receiverships and the Division of Administration, OI is leading the initiative to search the FDIC inventory of records. If the searches identify any possible records, we will review and provide that information to the appropriate FBI office.

[End of Office of Investigations Responds to Requests for Assistance in Terrorist Investigations panel]

As reported previously, the customer pleaded guilty in February of this year to bank fraud. The defendant's company had a floor plan agreement with MWSB which stipulated that he would remit proceeds from the sales of vehicles to the bank within one business day of the date of sale. During the period July 1998 through November 1999 the bank made 14 loans and subsequent renewals totaling \$153,000 to the company. The purpose of these loans was to purchase vehicles for resale. The loans were secured by 14 individually identified vehicles. The defendant subsequently sold these 14 vehicles without obtaining the bank's approval and failed to remit the proceeds from the sales as required.

We have reported several other actions resulting from these investigations that occurred in prior reporting periods. The president of a company was charged in several indictments last year with bank fraud, money laundering, and conspiracy to commit bank fraud and money laundering. In March of this year he pleaded guilty to one count of bank fraud and is currently awaiting sentencing. The former executive vice president of the bank pleaded guilty in August 2000 to a one-count information charging him with obstructing an examination of the financial institution and was sentenced in November to 12 months' probation and fined \$2,000. He also voluntarily signed a Stipulation and Consent to the Issuance of an Order of Prohibition From Further Participation, Section 8(e) of the Federal Deposit Insurance Act.

The investigations involving MWSB are being conducted jointly by the OIG, the FBI, and the

IRS, and the prosecutions are being handled by the U.S. Attorney's Office for the Southern District of Illinois.

Second Superseding Indictment Adds Additional Charges Against the Former Chairman of the Bank of Honolulu

On May 17, 2001, a federal grand jury in Honolulu returned a second superseding indictment against the former chairman and owner of

76 percent of the shares of the Bank of Honolulu, Honolulu, Hawaii. Five other individuals were also named in the latest indictment, including two of the former chairman's brothers, two of his business associates, and a female acquaintance. The new defendants are alleged in the indictment to have helped the former chairman hide money from the bankruptcy court and creditors.

Twelve of the 13 new charges in the latest indictment name the former chairman. They include three additional bankruptcy fraud counts, a charge of conspiracy to commit bankruptcy fraud, two counts of wire fraud, four counts of bank fraud, one count of causing a false statement to be made in the records of a financial institution, and a forfeiture count. The four bank fraud charges allege that he defrauded the bank of

\$6 million in loans by using false names to obtain loans and then transferring the proceeds to accounts he controlled. The forfeiture count seeks the forfeiture of approximately \$15 million in assets, including his \$4.6 million home in Bel Aire, California.

As reported previously, the former chairman was initially indicted in August 2000 on three counts of bankruptcy fraud. In October 2000, a superseding indictment added three additional counts of bankruptcy fraud and three counts of money laundering against him.

This case is being jointly investigated by the OIG and FBI and is being prosecuted by the U.S. Attorney's Office for the District of Hawaii.

Individual Pleads Guilty to Conspiracy to Defraud Several Financial Institutions and Is Sentenced

Following his plea of guilty in May to one count of conspiracy to defraud several financial institutions, a check counterfeiter was sentenced on July 27, 2001 in the Eastern District of Pennsylvania to 30 months' imprisonment and 36 months' supervised release and was ordered to pay full restitution of \$21,612 to the victims of his fraud scheme. The conspiracy charge was based on his participation in a counterfeit check scheme involving the negotiation or attempted negotiation of approximately five counterfeit FDIC checks. Our investigation, conducted jointly with the FBI and other members of the Philadelphia Bank Fraud Task Force, also identified seven non-FDIC counterfeit checks that the defendant and his accomplices deposited and/or cashed. The defendant was a fugitive from the time of his indictment in April 1999 until he was arrested on February 8, 2001 on narcotics charges in Philadelphia, Pennsylvania.

Our investigation was initiated after the FDIC learned that several individuals in the Philadelphia area had attempted to negotiate counterfeit FDIC checks at various financial institutions by depositing them in existing accounts and then later attempting to withdraw the

funds. The FDIC discovered the fraud when the checks were presented for payment because the check numbers had already cleared the system.

Former Loan Secretary Pleads Guilty to Embezzling from the Bank of Falkner

On September 20, 2001, a former loan secretary at the Bank of Falkner, Falkner, Mississippi, pleaded guilty in the District Court for the Northern District of Mississippi to a one-count Information charging her with embezzling \$21,040 from the bank. Her plea is pursuant to a plea agreement negotiated with the U.S. Attorney's Office for the Northern District of Mississippi.

The FDIC OIG is conducting a joint investigation with the FBI regarding suspected fraudulent activity that occurred at the Bank of Falkner prior to its failure on September 29, 2000. As a part of her plea agreement, the former loan secretary has agreed to cooperate with this ongoing investigation. Information obtained by the FDIC's Division of Resolutions and Receiverships during its post-closing review of the bank has significantly assisted the investigation.

Misrepresentations Regarding FDIC-Insurance

President and Owner of Investment Company Sentenced for Misapplication of Fiduciary Property and Securities Registration Violation; Additional \$2.2 Million of Investor Funds Recovered

On June 26, 2001, the president and owner of a San Antonio investment company was sentenced in Bexar County District Court, San Antonio, Texas, to 7 years' imprisonment, fined \$10,000, and ordered to pay \$8.2 million in restitution.

As reported previously, in February 2001 the defendant entered a plea of "nolo contendere" to selling unregistered securities and misapplication of fiduciary property. In exchange for his plea, the District Attorney for Bexar County agreed to dismiss the remaining four counts of a six-count indictment returned against him in June 2000 as well as nine other fraud-related indictments still outstanding against him. As essentially alleged in the indictments, the defendant advertised and sold certificates of deposit (CDs) paying relatively high rates of return through his investment company. In total, approximately \$9.1 million worth of CDs were sold to about 90 investors, most of whom were elderly. When investors bought the CDs, their contracts included a document giving control of the CD to the defendant. With control of the CDs, the defendant took them to Texas banks and used them as collateral for personal loans. He was alleged in the indictments filed against him to have engaged in fraud by intentionally failing to disclose that he transferred such proceeds to bank and brokerage accounts of businesses he controlled and used the proceeds for personal expenses and the purchase of a personal residence. Additionally, he was charged with misrepresenting that he was offering CDs that would be issued through an FDIC-insured bank, while knowingly omitting the material fact that any purported FDIC insurance would not protect investors from losses of their investment funds due to the defendant's default on his loans.

During the investigation, CDs totaling \$6,389,000 that were still being held at several San Antonio area banks were seized and the proceeds were used to repay the investors. The seizures forced the banks that were holding the CDs to seek restitution from the defendant. The banks responded that they should not be held responsible for the defendant's actions. Based on concerns raised as result of this case, the Texas Legislature adopted a new law

earlier this year that, in effect, lets banks freeze assets rather than permitting district attorneys to confiscate them by warrant. However, the bill also includes a provision that if banks refuse to comply with a search warrant, they can be held in contempt of court, and the culpable officers as well as the bank are liable.

Subsequent to the introduction of the new law in the Texas Legislature, the Bexar County District Attorney's office entered into agreements with Bank of America, Northwest Bank, and Clear Lake National Bank for the return of additional investor funds totaling approximately \$2.27 million that had been deposited by the defendant as a part of the same scheme.

This case was investigated by the OIG and the Texas State Securities Board and was prosecuted by the Bexar County District Attorney's Office, San Antonio, Texas.

San Antonio Investment Broker Sentenced in Connection with Fictitious Certificate of Deposit Program; Additional \$90,000 of Investor Funds Recovered

On April 23, 2001, the owner of an investment broker company located in San Antonio, Texas, was sentenced in the Bexar County District Court to 15 years' imprisonment, fined \$1,000 and ordered to pay \$382,985 in restitution. The sentencing followed his prior guilty plea in January to one count of second degree theft and one count of first degree securities fraud under the Texas Penal Code.

As reported previously, the defendant had been charged in a June 2000 indictment with securities fraud, misapplication of fiduciary property, theft, and securing execution of a document through deception. The indictment charged that he had engaged in fraud by misrepresenting to six investors that Bank of America (BOA) CDs totaling over \$334,600 were issued in their names. In doing so he also falsely misrepresented that the CDs were FDIC-insured. In fact, the six CDs were issued in the name of his company on BOA's records and then pledged as collateral on loans. When the defendant subsequently defaulted on the loans, the collateral was forfeited. Additionally, relative to a seventh individual, the defendant was charged with (1) misapplying over \$100,000 that he held as a fiduciary on behalf of the individual, (2) unlawfully appropriating over \$100,000 of the individual's money, and (3) causing the individual to execute a document by deception affecting over \$100,000 of his money. The indictment also charged that he had not disclosed to the investors that he had been convicted of felony theft in 1987 and securities fraud in 1993.

On March 30, 2001, an agreement was reached between BOA and the Bexar County District Attorney's Office whereby BOA agreed to return funds totaling \$90,000 that were invested with the broker by two of his victims.

The defendant's former accomplice at BOA pleaded guilty to federal criminal charges in connection with this case and was sentenced to 15 months' imprisonment to be followed by 36 months' probation. He is still awaiting resolution of a possible order of restitution that was postponed during his January 2001 sentencing in the Western District of Texas.

This case was investigated by the OIG, the FBI, and the Texas State Securities Board and is being prosecuted by the Bexar County District Attorney's Office and the U.S. Attorney's Office for the Western District of Texas.

Restitution and Other Debt Owed the FDIC

Real Estate Trustee Pleads Guilty to Illegally Diverting FDIC Funds and Is Ordered to Pay \$100,000 Fine

On September 20, 2001, a Massachusetts attorney pleaded guilty in the U.S. District Court for the District of Massachusetts to a superseding Information charging him with knowingly, willfully, and unlawfully converting to his personal use things of value of the FDIC. After entering his plea he was sentenced to pay a fine of \$100,000.

As previously reported, the defendant, who was formerly a member of Congress and a Director of the Federal Reserve Bank of Boston, was charged in a 12-count Information in January 2000 with submitting fraudulent financial statements to several financial institutions and the FDIC. As a part of a plea agreement with the U.S. Attorney's Office for the Eastern District of Massachusetts, the charges in the pending 12-count indictment were dismissed in return for his guilty plea.

The plea relates to the defendant's conduct as the Trustee of Three Corners Realty Trust, which owned the Hawthorne Hotel. Funds of the hotel were pledged as collateral for a \$6.25 million loan the hotel obtained from the Bank of New England, for which the FDIC was appointed receiver following its failure. In a separate statement of facts that was filed as part of the plea agreement, the defendant admitted that over the period January 1991 to December 1993 he wrongfully converted \$226,771 in funds to his personal use. On 151 occasions over the 3-year period, he endorsed checks as trustee of the realty trust and deposited the checks into his personal checking accounts for his personal use. He also admitted to submitting personal financial statements to RECOLL, an agent for the FDIC, from which he intentionally omitted any reference to the funds he was wrongfully taking out of the hotel. The defendant also repaid \$200,000 to the FDIC in June 1995 as part of an offer to compromise the Hawthorne Hotel loan.

This investigation was conducted jointly by the FDIC OIG and the FBI.

Strawbuyer Pleads Guilty to Perjury

On June 27, 2001, a financial facilitator entered a plea of guilty in U.S. District Court for the District of Massachusetts to one count of making a false declaration to a federal grand jury.

During the late 1970's and through the early 1990's, the defendant served as a commercial loan officer for several financial institutions. He also worked for a short time in Resolution Trust Corporation (RTC) receiverships and was a workout specialist with the RTC/FDIC Franklin Office. In 1994 he agreed to a removal order issued by the FDIC prohibiting him from participating in the conduct or affairs of, or exercising voting rights in, any insured institution without the prior consent of the FDIC. Subsequently, he began providing services to individuals who owed money to the FDIC and RTC to help them work out their debts. His plea of guilty to perjury was in connection with his testimony before a federal grand jury that is investigating purchases of assets from the FDIC. The defendant purchased an asset from the FDIC in 1994 and resold it 4 months later to the original owner.

The FDIC OIG initiated this investigation as a part of its participation in the now-disbanded New England Bank Fraud Task Force. As a part of his plea agreement, the defendant must

cooperate with investigators who are continuing to review the activities of others involved in purchases of FDIC assets.

Strawbuyer in Loan Fraud Scheme Is Sentenced

On July 26, 2001 a strawbuyer who was involved in a scheme with three developers to repurchase defaulted loans at a discount was sentenced in the U.S. District Court of Arizona to 4 years' probation and fined \$5,000. The defendant had previously pleaded guilty in February to tax evasion. As a part of his plea agreement, he also paid the FDIC \$250,000 to settle all claims against him in connection with his involvement in the scheme.

As previously reported, the three developers involved in the scheme were sentenced to pay fines totaling \$212,820 and restitution totaling \$7,243,220. Payment of the restitution was split with \$1.5 million going to the FDIC and the remaining \$5.7 million going to the IRS to resolve tax problems. Additionally, each of the three was sentenced to 24 months' probation and ordered to perform 400 hours of community service.

The prosecutions in this case were the result of a joint FDIC and IRS investigation into allegations that the developers committed tax fraud and provided false financial statements to the former RTC and an RTC contractor in connection with two non-performing loans the three had with a failed thrift. Our investigation found the developers were guarantors on two loans totaling \$15.9 million from Empire of America Realty Funding Corporation, a subsidiary of Empire of America Federal Savings Bank, Buffalo, New York. The loans originated in 1988 and 1989 and were to be utilized for the construction of two apartment complexes.

In 1990, the RTC was appointed conservator of Empire and acquired the two delinquent loans. In early 1991, the developers requested loan modifications that the RTC denied. In late 1991, the developers repurchased their loans for \$9 million from the RTC using a strawbuyer. The sale resulted in a loss of over \$6 million. The developers subsequently sold the apartment complexes at a profit of \$8 million and failed to report the gain to the IRS.

The investigation revealed the developers submitted false financial statements to the RTC which the RTC contractor relied on as a basis for its decision not to pursue the developers' guaranties. The financial statements represented that the developers' net worth was insufficient to recover on the guaranties.

Former Contract Auctioneer Indicted for Credit Card Fraud and Concealing Assets to Avoid Paying Restitution to the FDIC

On August 16, 2001, a former contractor who was previously investigated by the OIG and convicted of embezzling funds from the RTC was indicted by a grand jury in the Southern District of Florida, Miami, Florida, on charges of credit card fraud and concealing assets to avoid paying restitution to the FDIC.

In April 2000 the contractor was sentenced to serve 5 months of confinement, 150 days of home detention, and 1 year of probation and to pay a fine of \$75,000. Also as a part of the sentencing, he and his company were ordered to pay restitution jointly and severally of \$118,130 to the FDIC.

In the most recent indictment, the contractor is alleged to have concealed assets to avoid

paying the restitution to the FDIC. Specifically, he is alleged to have transferred his interest in his home via a quit claim deed to his wife within days after learning of an imminent potential indictment against him in the embezzlement case. He is further alleged to have agreed as a part of his subsequent divorce that his wife would receive any and all proceeds from the sale of the home. The home was sold in May 2000 for a net profit of \$663,396. The indictment states that the defendant told his probation officer in May 2000 that he had no funds to pay any of the restitution because of the terms of the divorce.

The investigation that resulted in the most recent indictment was conducted jointly with the U.S. Secret Service. Based on information obtained during the investigation, the defendant was also indicted on one count of credit card fraud.

Contractor Activities

Contractor Principals Indicted for Conspiracy and Submitting False Statements to the FDIC

On April 6, 2001, two principals of an FDIC contractor were indicted by a federal grand jury in the Middle District of Florida, Tampa, Florida, on one count of conspiracy and three counts of making/submitting false statements to the FDIC.

This indictment is the result of an investigation initiated by the Department of Justice and the OIG based on allegations contained in a civil complaint filed by a private citizen under the False Claims Act. The indictment alleges that the two individuals, on behalf of Golden Ocala Golf Course Partners, submitted three false invoices and bogus support documentation to the FDIC. These documents purported that Golden Ocala Golf Course Partners, a contractor hired by the FDIC, had paid a nonexistent company \$240,000 for environmental remediation work that was actually performed by other companies at a total cost of \$51,376.25. Based on this false documentation, the FDIC reimbursed the partnership \$150,000 for expenses.

As previously reported, in September 2000 one of the partners entered into an agreement wherein he will pay the government \$300,000 to settle the civil complaint.

Former RTC Contractor Sentenced to Pay the FDIC \$300,000 in Connection with Bank Fraud Violations

On July 18, 2001, the holding company of a former RTC contractor was sentenced in United States District Court for the Middle District of Florida, Orlando, Florida, to pay the FDIC as receiver of two institutions that were taken over by the RTC a total of \$300,000. The sentencing of the company followed its prior agreement in April 2001 to plead guilty to a single count of bank fraud. As part of the plea agreement the holding company will be dissolved.

The contractor repossessed and sold leased vehicles for RTC conservatorship institutions. The investigation was initiated based on information from a former employee of the contractor who alleged that the company submitted fraudulent bids regarding the repossession and ultimate sale of vehicles. The investigation disclosed that the company submitted fictitious bid sheets to the lien holders of repossessed vehicles and kept the additional funds derived from the actual higher price for which the vehicles were sold.

The investigation was conducted by the FDIC OIG, and the prosecution is being handled by the U.S. Attorney's Office, Orlando, Florida.

Former FDIC Contractor Sentenced for Conspiracy and Obstructing an OIG Audit

On May 21, 2001, a former FDIC contractor was sentenced in Federal District Court, Orlando, Florida, to 2 years' probation, fined \$2,500 and ordered to forfeit \$8,908. The contractor had previously been indicted in September 2000 on 38 counts of various types of criminal activities and pleaded guilty in February 2001 to conspiracy and impeding the functions of the FDIC by obstructing an OIG audit.

As previously reported, the former FDIC contractor had been retained to manage the Shelter Cove R.V. Resort, an FDIC-owned property in St. Cloud, Florida. The contractor formed a partnership with a subcontractor he had hired to perform repairs at Shelter Cove. The contractor and the subcontractor then shared the proceeds of funds received from the FDIC for payment of repair expenses. The contractor was charged with failing to disclose his affiliation with the partnership to the FDIC or to OIG auditors and with submitting false and forged bids from other purported contractors for work at Shelter Cove. The sentencing of the contractor completes the investigation and prosecution of this case.

Former FDIC Contractor Employee and an Accomplice Are Sentenced in Connection with Thefts of FDIC Laptop Computers

A former employee of an FDIC contractor pleaded guilty in April to a charge of conspiracy in connection with his participation in the theft and resale of laptop computers belonging to the FDIC. In June he was sentenced in the U.S. District Court for the Eastern District of Virginia to 4 months' home detention, 36 months' probation, and ordered to pay \$42,950 restitution to the FDIC. His accomplice in the scheme, who had also pleaded guilty to conspiracy, was sentenced in May to 3 years' probation and ordered to pay \$40,000 restitution to the FDIC.

The investigation of the laptop thefts was initiated by the OIG based on a referral from the Division of Information Resources Management (DIRM) stating that a laptop computer was missing and possibly stolen. The computer in question was part of the FDIC computer equipment inventory under the control of an FDIC contractor responsible for inventory management. As described in documents filed with the court in this case, the defendant used his position as an employee of the FDIC contractor to steal computers belonging to the FDIC. His accomplice assisted in selling the stolen computers to unsuspecting third parties for approximately \$600 to \$1,200 each. Between approximately October 1998 and December 1999, at least 50 FDIC computers were stolen. FDIC OIG Special Agents have recovered 36 of the stolen computers.

Employee Activities

Former FDIC Employee Sentenced for Her Role in Identity Fraud Scheme

A former employee in the FDIC Division of Finance was sentenced on May 29, 2001, in the U.S. District Court of Maryland to 5 years' probation, including 6 months' home confinement, and was ordered to pay \$87,531 in restitution. Her sentencing was based on her prior plea of guilty in March 2001 to conspiracy in connection with an identity fraud scheme. The scheme's victims included employees of the FDIC and the Department of Health and Human Services

(HHS).

As reported previously, from August 1999 through June 2000, the defendant conspired with five others to obtain goods and services on credit by using the names and personal information of unwitting victims. She admitted that the conspirators obtained fraudulent identification cards in the victims' names and used the names to open credit accounts, obtain goods and services in retail stores, and order merchandise over the Internet. Purchases included gift certificates, jewelry, and electronic equipment. In furtherance of the conspiracy, the former FDIC employee checked the victims' credit status by applying for credit accounts using the victims' names, Social Security numbers, and other identifying information.

This case was investigated by the Inspectors General of the FDIC and the HHS and was prosecuted by the U.S. Attorney's Office for the District of Maryland.

Misuse of Corporate Credit Card Results in Employee's Resignation and Revised Management Controls

An investigation conducted by the OIG at the request of the FDIC's Division of Administration (DOA) resulted in the resignation of a Dallas employee who was reported to have used the Corporation's Visa credit card to make unauthorized purchases.

Specifically, it was determined that between 1999 and 2000 the former DOA employee purchased \$5,000 in unofficial and/or personal items using the card. Of that amount, \$1,500 was spent on toys allegedly given to the Toys for Tots campaign. The employee claimed that her purchases were made at the instruction of her supervisor; however, many of the items either remained in the employee's personal possession or could not be accounted for by the FDIC. The employee voluntarily returned a number of items to the FDIC and a consensual search of the former employee's residence by the OIG also resulted in the recovery of several additional items.

While prosecution of the employee was declined by the United States Attorney's Office, the investigation did result in added DOA oversight and the implementation of new controls regarding the use of FDIC corporate credit cards.

[End of the Investigations Section of the Semiannual Report]

[Start of the OIG Organization Section of the Semiannual Report]

OIG Organization

The OIG continued its quest for high performance and effectiveness with several initiatives during this period. At the forefront, the OIG reorganized its Office of Audits and merged its evaluation unit into the office to more effectively use resources and respond to corporate needs. Mr. Russell Rau was hired during the period to be our Assistant Inspector General for Audits. Also, the OIG established an Office of Policy Analysis and Congressional Relations to provide the Congress and agency management with analyses of policy issues impacting the operations of the Corporation and the financial services industry. Mr. David Loewenstein has been appointed Assistant Inspector General for Policy Analysis and Congressional Relations. The OIG's new organization chart is shown in this section.

The OIG has taken several initiatives to improve its use of technology. We continued efforts to establish an in-house computer forensic capability to meet the growing need for OIG special agents to acquire and examine evidence from suspect computers. In addition, our office invested in new laptops and docking stations that give our auditors and investigators access to technology almost anywhere their work leads them, including telework locations. In line with the Corporation, we have also established the position of an OIG Information Security Manager whose responsibility will include establishing a security program to manage and mitigate the internal risks inherent with the growing use of computer technologies.

The OIG continued to invest in its most important asset—the men and women who comprise our audit, investigation, legal, and administrative staff. About 90 percent of our budget resources are spent on compensation and training for our staff. We have started an initiative to develop a Human Capital Strategic Plan to lay out our long-term strategies for managing this most vital asset. In addition, we have put the final touches on plans for an OIG-wide conference under the theme Putting People First, which is scheduled for October 22-26 in Portsmouth, Virginia. Our office also participated with other FDIC offices in a Diversity Day celebration that was an educational opportunity for Washington area staff to learn about different cultures that make up the FDIC workforce.

Reorganizations Set Stage for Higher Performance

Our newly reorganized Office of Audits aligns staff more along functional lines than our previous organization had done. Instead of organizationally distinct field offices, the staff in those offices are assigned to specific functions along with headquarters staff. The principal functional areas are Supervision, Insurance, and Consumer Affairs; Information Assurance; Financial Management; Receivership Management; Contracting, Administrative, and Legal Services; and Corporate Evaluations. Additionally, the Audit Quality directorate works to ensure quality in all audit processes and products.

Assisting Mr. Rau in the leadership of the office are two FDIC veterans.

Ms. Sharon Smith and Mr. Steve Beard are Deputy Assistant Inspectors General. Ms. Smith has spent 27 years performing FDIC audits. Mr. Beard formerly headed the OIG evaluation and congressional relations functions for both the FDIC OIG and the former Resolution Trust Corporation OIG.

Our new Office of Policy Analysis and Congressional Relations will conduct analyses that reflect the unique perspective of the OIG and provide policymakers with information to assist them in implementing policy that efficiently and effectively advances the accomplishment of the agency's mission, protects the viability of the insurance funds, and allows for an objective evaluation of policy implementation. The office also is responsible for managing the OIG's relations with the Congress and serves as the OIG liaison and point-of-contact for congressional matters, including contacts with both the Congress and the FDIC's Office of Legislative Affairs. In laying the groundwork for the new office, we contacted key staff members of our congressional oversight committees, which strengthened the committees' understanding of the OIG's work and what it is the OIG offers the Congress. This office will be staffed with individuals having expertise in auditing, program/policy analysis, and/or banking and economics.

Putting Technology to Work and Improving Electronic Security

Computer forensic examinations are becoming more critical in those situations where the crime under investigation involves the use of computers. Acquiring the evidence needed is no easy task when considering the variety of computer configurations and storage media existing today. Our Office of Investigations established an Electronic Crimes Team to provide technology assistance to OIG investigations. The team assists with:

- Developing criminal investigations, including electronic media search warrants and subpoenas.
- Providing on-site field support for executing search warrants, physically seizing electronic hardware, and initial reviews of electronic media.
- Providing laboratory analysis and court testimony concerning electronic evidence.

The Electronic Crimes Team uses highly specialized forensic hardware and software that is the latest technology available to assist law enforcement in performing these types of criminal investigations.

Another useful work tool has emerged in our workplace. Both our investigators and auditors will be able to work more effectively with the OIG's new laptop docking stations. These computers enable our staff to take their computers with them when they travel or need to go to another office. They have also proved to be a valuable tool in the OIG's telework program. These computers work either as stand-alone computers or connected to the FDIC network, which can be accomplished either directly at the docking station on a person's desk or remotely via a telephone modem connection. These computers complement new software that we have purchased from the public accounting firm, PriceWaterhouseCoopers, for our auditors to automate their working papers, allowing for better quality and efficiency. Our staff will be trained in the use of the software in the upcoming year.

In the face of rapid technological innovations, one of the FDIC's primary challenges has been managing the evolution of its Information Security Program within the Corporation. Additionally, a number of new federal laws and regulations have emerged, including Presidential Decision Directive #63, "Protection of Critical Infrastructure," which addresses the need for enhanced security controls as organizations continue their growing reliance on business functions that are supported by information technology. During the reporting period, the OIG established a full-time Information Security Manager to be responsible for managing the development and implementation of the OIG's Information Security Program.

Aligning Human Resources to Support the OIG Mission

The OIG's people—its human capital—are its most critical assets. The OIG's ability to produce audits, investigations, and other products and serve clients and other stakeholders is directly linked to the quality of our leadership team, the abilities of our staff, and a work environment that supports high performance. Like many other organizations, we face increasing pressures to deliver with greater value, timeliness, and quality. As the value of our people increases, so does the performance capacity of the OIG and, therefore, our value to clients and other stakeholders. Recognizing these realities has led us to begin developing a *Human Capital Strategic Plan*.

The OIG's Human Capital Strategic Plan will complement the OIG's Strategic Plan by

aligning and integrating human resources policies and practices to support our mission. We are building our plan around a self-assessment framework published by the U.S. General Accounting Office (GAO), with modifications to address the aspects of our human resources policies and practices that we believe can be leveraged to enhance a results-oriented performance culture in the OIG.

The OIG's October 2001 conference for all its staff will reinforce the themes being built into the human capital plan. The conference theme, Putting People First, reflects the value the OIG places on its staff and the role they have in contributing to the FDIC and OIG missions. Speakers will discuss GAO's human capital strategies, the attributes of high performance organizations, the importance of staff diversity, the significance of differing personality types, and author Steven Covey's seven habits of highly effective people.

[Contained in the OIG Organization section of the report is a panel titled - "FDIC Inspector General Leads IG Community Initiatives"]

[Start of FDIC Inspector General Leads IG Community Initiatives panel]

FDIC Inspector General Leads IG Community Initiatives

Over the last 6 months, the Inspector General (IG) community continued its education focus, both at home and abroad. The FDIC Inspector General, serving as Vice Chair of the President's Council on Integrity and Efficiency, believes that sharing the community's knowledge and experience will pay dividends throughout the government.

In May 2001, the IG community adopted A Strategic Framework to lay out a strategy for fulfilling their agency missions as well as collectively contributing to resolving government-wide challenges. A Progress Report to the President, the community's annual report, was published in July 2001, as discussed on the inside back cover of this report. Roundtables established to share ideas and best practices on crosscutting issues, such as performance and results, information technology, and teleworking, continued to flourish.

On the global front, the FDIC Inspector General met with three delegations of international visitors to share experiences and provide materials on the IG concept. Although the groups were diverse in terms of nationality, background, education, and profession, they shared some significant common challenges, such as effecting changes in their government, operating independently, and instilling integrity in programs and operations. During these uncertain times, stability of international governments is critical, and the IG community welcomes opportunities to contribute its perspectives.

[End of FDIC Inspector General Leads IG Community Initiatives panel]

[Contained in the OIG Organization section of the report is a panel titled - "OIG Internal Activities"]

[Start of OIG Internal Activities panel]

OIG Internal Activities

- Seven OIG special agents responded to a request from the Federal Bureau of Investigation (FBI) and the Department of Defense to work on the evidence recovery team at the site of the Pentagon terrorist attack. Additionally, two agents have been assigned to work with the FBI in New York.

- Reorganized the OIG's Office of Audits.

- Hired Russell Rau as Assistant Inspector General for Audits.

- Established OIG Office of Policy Analysis and Congressional Relations.

- Conducted training and launched OIG telework program, permitting OIG staff to work from remote locations with supervisory approval.

- Completed internal quality assurance reviews of Office of Audits and Office of Congressional Relations and Evaluations.

- External peer review begun of the OIG's Office of Audits by the OIG at the Agency for International Development.

- Initiated the process to update the OIG's strategic and annual performance plans.

- Deployed laptop/docking station computers to most OIG staff.

- Purchased software to automate auditor working papers to improve the quality and efficiency of OIG audits.

- Established the OIG's Electronic Crimes Team to provide technology assistance to investigations conducted by OIG special agents.

- Appointed an OIG Information Security Manager to manage the development and implementation of an OIG information security program.

- Began development of an OIG Human Capital Strategic Plan to align human resources policies and practices to support the OIG mission.

- The Inspector General and several staff attended the Association of Government Accountants' Annual Professional Development Conference and Exposition.

- The Inspector General co-chaired a track for the E-Gov 2001 International Conference and Exposition that was held from July 9-12, 2001 in Washington, D.C. The track explored how professionals in domestic law enforcement groups, the military, and international authorities employ e-government strategies to analyze, share, and distribute information for enforcing regulations and preventing criminal and terrorist activities.

- OIG staff attended the fourth annual Performance Conference sponsored by the National Academy of Public Administration, which focused on performance-related initiatives of the new administration.

- The Inspector General attended the Excellence in Government 2001 conference along with one of the Deputy Assistant Inspectors General for Audits. This conference brought together hundreds of government executives eager to address and learn more about such issues as human capital challenges, e-government, leadership, measuring and managing performance, and achieving innovation and results through partnerships.
- The Assistant Inspector General for Investigations and other OIG staff attended the National Organization of Black Law Enforcement Executives (NOBLE) Conference, which provided an opportunity for professional growth and interaction with other law enforcement professionals.
- The Inspector General attended a National Intergovernmental Audit Forum meeting on August 29 –30. The forum is led by the U.S. General Accounting Office (GAO) and includes federal, state, and local government auditors. Topics at this forum were the current status of updating the auditor independence standard, the importance of computer security, how to audit service contracts, and the management of human capital.
- The Inspector General continued to serve as a member of the Advisory Council on Government Auditing Standards to update GAO's government auditing standards.
- Two OIG teams have been selected to receive Awards for Excellence by the President's Council on Integrity and Efficiency. Receiving the awards are a joint FDIC/FBI

investigative team who have participated in the fraud case at First National Bank of Keystone and the evaluation team that reviewed the FDIC's nationwide telecommunications

contract. Also, Russell Rau is being recognized with an Award for Excellence for his exemplary leadership and service to the Inspector General community in his capacity as Chair of the Federal Audit Executive Council.

- OIG Counsel's office actively litigated 13 matters during the reporting period. Such matters involved the Equal Employment Opportunity statute, the right to Financial Privacy Act, the qui tam provisions of the False Claims Act, whistleblower protection laws, and civil and criminal cases in which OIG documents were sought in discovery. These matters are in addition to matters that are awaiting further action by the parties or rulings by the courts or other adjudicatory bodies.
- OIG Counsel's office provided advice and counseling, including written opinions, on a number of issues, including the implications of the Privacy Act and Rehabilitation Act section 508 on OIG systems, the Government Information Security Reform Act, the Federal Advisory Committee Act, the Buy America Act, interpretation of various Office of Management and Budget circulars, unclaimed deposits, copyright matters, investigative matters, contract interpretations and consulting issues, housing discrimination, disclosure of information, the Bank Secrecy Act, union-related matters, theft of computer equipment, and various ethics-related matters.

[End of OIG Internal Activities panel]

[Contained in the OIG Organization section of the report is a panel titled - "Coordination with and Assistance to FDIC Management"]

[Start of Coordination with and Assistance to FDIC Management panel]

Coordination with and Assistance to FDIC Management

- The Inspector General briefed new FDIC Chairman Donald E. Powell on the OIG's role and mission.

- The OIG provided weekly highlights reports to the Chairman summarizing key OIG activities.

- An OIG team developed an exhibit showing the diverse background of our staff with maps showing states where our staff were born and lived as well as countries of

family origins, which was shared with other FDIC staff at a Diversity Day function for all Washington employees. OIG staff have participated in similar events around the country where we have offices.

- The OIG participated in the Office of Internal Control Management's (OICM) contractor summit meeting and worked proactively with other FDIC offices to correct contract oversight problems.

- The Assistant Inspector General for Quality Assurance and Oversight and other staff met with the Division of Research and Statistics to discuss program evaluation requirements under the Government Performance and Results Act.

- OIG staff conducted quarterly status briefings for officials of the Division of Resolutions and Receiverships by summarizing each ongoing survey and audit and updating project status.

- The Assistant Inspector General for Investigations and other special agents participated in training sessions on white-collar crime at a Division of Supervision regional training conference in St. Louis, Missouri.

- The Counsel to the Inspector General presented information about OIG civil and criminal investigations at the Legal Division's Professional Liability and Financial Crimes Unit's continuing legal education program in Dallas, Texas.

- Audit staff gave presentations on Internet fraud at a Division of Finance conference in Baltimore, Maryland.

- One of the OIG's audit managers provided assistance requested by the Division of Finance in writing new policies covering working paper documentation in bank examinations and reviews of internal routines and controls, both having been subjects of recent OIG audits.

- The OIG's Office of Quality Assurance and Oversight provided advisory comments to the Division of Finance pertaining to the draft 2001-2006 FDIC Strategic Plan.

- Representatives from the OIG, Division of Supervision, and Office of Legislative Affairs met with staff of the House Committee on Financial Services to brief them on supervisory issues and a criminal investigation related to a community bank.

- OIG special agents made presentations about various automated teller machine fraud schemes at the Division of Supervision's regional training conference in Portland, Oregon.
- The OIG's evaluations unit and OICM jointly conducted a review of the FDIC's corporate planning cycle at the request of the Chief Financial Officer. We made recommendations for streamlining planning efforts to reduce workload burdens.
- Issued interim results of our audit of the FDIC's Surplus Computer Program, advising management of concerns related to the FDIC's program for disposing of excess computers.
- The OIG completed an annual review of the Corporation's Internal Control and Risk Management Program, concluding that the program was conducted in accordance with FDIC policy and was consistent with provisions of the Federal Managers' Financial Integrity Act. We also provided OICM advisory comments regarding changes to the Internal Control Program.

[End of Coordination with and Assistance to FDIC Management panel]

OIG Organizational Chart

Immediate Office: Inspector General, Deputy Inspector General

Counsel to the Inspector General: reports directly to the Inspector General

Offices of the Inspector General are comprised of : Office of Audits, Office of Investigations, Office of Policy Analysis and Congressional Relations, Office of Management and Policy, Office of Quality Assurance and Oversight. Each office is headed by an Assistant Inspector General.

[Photo of Rus Rau, Assistant Inspector General for Audits, precedes this section]

Mr. Russell A. Rau has joined the FDIC OIG as its Assistant Inspector General for Audits. Mr. Rau comes to our office from the OIG at the National Aeronautics and Space Administration (NASA) where he had also been the Assistant Inspector General for Audits since 1998. He previously held several positions with the Department of Defense OIG. He has also served as Chair of the Federal Audit Executive Council. Mr. Rau is a Certified Public Accountant, Certified Internal Auditor, and Certified Information Systems Auditor. He earned his Bachelor and Master of Science degrees in accounting from the State University of New York at Albany.

[Photo of David Loewenstein, Assistant Inspector General for Policy Analysis and Congressional Relations, precedes this section]

Mr. Loewenstein was appointed as Assistant Inspector General for Policy Analysis and

Congressional Relations. He previously served as the Assistant Inspector General for Headquarters Audits in FDIC’s OIG. He joined the OIG in 1989. Prior to 1989, he had been the Deputy Inspector General at the former Federal Home Loan Bank Board OIG. Mr. Loewenstein is a Certified Public Accountant. He is a graduate of the University of Illinois where he was awarded his Bachelor’s degree in accounting. He earned his Master’s degree in business administration from The George Washington University.

[Photo of OIG Executives- (standing, left to right) David Loewenstein, Russell Rau, Gaston Gianni, Patricia Black, Samuel Holland, Rex Simmons (sitting, left to right) Stephen Beard, Sharon Smith, Robert McGregor]

Table 1: Significant OIG Achievements for the period April 1, 2001 - September 30, 2001. 7 Audit Reports Issued. 8 Audit-Related Memorandums Issued *. 2 Evaluation Reports Issued. 3 Evaluation-Related Correspondence Issued *. Questioned Costs and Funds Put to Better Use from Audit and Evaluation Reports - None this period. 15 Investigations Opened. 21 Investigations Closed. 44 OIG Subpoenas Issued. 10 Convictions. \$11.8 million in Fines, Restitution, and Monetary Recoveries. 10 Hotline Allegations Referred. 15 Allegations Substantiated. 4 Allegations Closed. 3 Proposed or Existing Regulations and Legislation Reviewed. 22 Proposed FDIC Policies and Directives Reviewed. 4 Responses to Requests and Appeals Under the Freedom of Information Act and Privacy Act 4. *Footnote - These memorandums and other correspondence relate to OIG work that did not result in formally issued audit or evaluation reports.

[Photo of OIG Summer 2001 Interns- front row left to right- C. Pollard, N. Wilson, S. Farooqi. Back row left to right- M. Gilhooly, H. Albert, IG Gianni, C. Veasey, E. Martin]

Table 2: Nonmonetary Recommendations. From April 1999 to September 1999, there were 66. From October 1999 to March 2000 there were 68. From April 2000 to September 2000 there were 74. From October 2000 to March 2001 there were 90. From April 2001 to September 2001 there were 34.

Figure 1: Graph of Products Issued and Investigations Closed - From April 1999 to September 1999 there were approximately 31 audits and evaluations. From October 1999 to March 2000 there were approximately 37 audits and evaluations. From April 2000 to September 2000 there were approximately 53 audits and evaluations. From October 2000 to March 2001 there were approximately 43 audits and evaluations. From April 2001 to September 2001 there were approximately 20 audits and evaluations. From April 1999 to September 1999 there were approximately 30 investigations. From October 1999 to March 2000 there were approximately 32 investigations. From April 2000 to September 2000 there were approximately 34 investigations. From October 2000 to March 2001 there were approximately 42 investigations. From April 2001 to September 2001 there were approximately 21 investigations.

Figure 2: Questioned costs/funds put to better use as a result of audits and evaluations - From April 1999 to September 1999 there were approximately \$16 million. From October 1999 to March 2000 there were approximately \$4 million. From April 2000 to September 2000 there were approximately \$11 million. From October 2000 to March 2001 there were approximately \$7.5 million. There were none during the period from April 2001 to September 2001.

Figure 3: Fines, restitutions, nad monetary resoveries resulting from OIG investigations - From April 1999 to September 1999 there were approximately \$11 million. From October

1999 to March 2000 there were approximately \$14 million. From April 2000 to September 2000 there were approximately \$10 million. From October 2000 to March 2001 there were approximately \$65 million. From April 2001 to September 2001 there were approximately \$10.5 million.

Table 3: **OIG Review of Proposed or Existing Legislation and Regulations.** (April 1, 2001 - September 30, 2001) The Counsel's office carried out its responsibilities under the Inspector General Act to review proposed or existing legislation and regulations. During this reporting period, we reviewed and provided comments on the draft version of the Request for Public Comments on Rules changes needed for electronic banking.

We also commented on S. 1371, the "Money Laundering Abatement Act," by addressing a statute of limitation issue, seeking clarifications of the (1) Right to Financial Privacy Act relative to money laundering investigations and (2) the Secretary of the Treasury's ability to establish, by regulation, lower thresholds of what constitutes a "private bank account" under this bill.

In addition to the bills we reviewed, we also provided to the Congress a draft legislative proposal which would rescind the requirement in current law requiring the General Accounting Office to audit the FDIC's financial transactions. Financial statement audits would continue to be done under the Chief Financial Officers Act.

Reporting Terms and Requirements

Index of Reporting Requirements - Inspector General Act of 1978, as amended

Reporting Requirement Page: Section 4(a)(2) - Review of legislation and regulations - page 39, Section 5(a)(1) - Significant problems, abuses, and deficiencies pages 11-24, Section 5(a)(2): Recommendations with respect to significant problems, abuses, and deficiencies pages 11-24, Section 5(a)(3) - Recommendations described in previous semiannual reports on which corrective action has not been completed page 42, Section 5(a)(4) - Matters referred to prosecutive authorities page 25, Section 5(a)(5) and 6(b)(2) - Summary of instances where requested information was refused page 48, Section 5(a)(6) - Listing of audit reports page 46, Section 5(a)(7) - Summary of particularly significant reports pages 11-24, Section 5(a)(8) - Statistical table showing the total number of audit reports and the total dollar value of questioned costs page 47, Section 5(a)(9) - Statistical table showing the total number of audit reports and the total dollar value of recommendations that funds be put to better use page 47, Section 5(a)(10) - Audit recommendations more than 6 months old for which no management decision has been made page 48, Section 5(a)(11) - Significant revised management decisions during the current reporting period page 48, Section 5(a)(12) - Significant management decisions with which the OIG disagreed page 48.

Reader's Guide to Inspector General Act Reporting Terms

What Happens When Auditors Identify Monetary Benefits?

Our experience has found that the reporting terminology outlined in the Inspector General Act of 1978, as amended, often confuses people. To lessen such confusion and place these terms in proper context, we present the following discussion:

The Inspector General Act defines the terminology and establishes the reporting requirements for the identification and disposition of questioned costs in audit reports. To understand how this process works, it is helpful to know the key terms and how they relate to each other.

The first step in the process is when the audit report identifying **questioned costs*** is issued to FDIC management. Auditors question costs because of an alleged violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other agreement or document governing the expenditure of funds. In addition, a questioned cost may be a finding in which, at the time of the audit, a cost is not supported by adequate documentation; or, a finding that the expenditure of funds for the intended purpose is unnecessary or unreasonable.

The next step in the process is for FDIC management to make a decision about the questioned costs. The Inspector General Act describes a "**management decision**" as the final decision issued by management after evaluation of the finding(s) and recommendation(s) included in an audit report, including actions deemed to be necessary. In the case of questioned costs, this management decision must specifically address the questioned costs by either disallowing or not disallowing these costs. A "**disallowed cost**," according to the Inspector General Act, is a questioned cost that management, in a management decision, has sustained or agreed should not be charged to the government.

Once management has disallowed a cost and, in effect, sustained the auditor’s questioned costs, the last step in the process takes place which culminates in the "**final action**." As defined in the Inspector General Act, final action is the completion of all actions that management has determined, via the management decision process, are necessary to resolve the findings and recommendations included in an audit report. In the case of disallowed costs, management will typically evaluate factors beyond the conditions in the audit report, such as qualitative judgements of value received or the cost to litigate, and decide whether it is in the Corporation’s best interest to pursue recovery of the disallowed costs. The Corporation is responsible for reporting the disposition of the disallowed costs, the amounts recovered, and amounts not recovered.

Except for a few key differences, the process for reports with recommendations that **funds be put to better use** is generally the same as the process for reports with questioned costs. The audit report recommends an action that will result in funds to be used more efficiently rather than identifying amounts that may need to be eventually recovered. Consequently, the management decisions and final actions address the implementation of the recommended actions and not the disallowance or recovery of costs.

* It is important to note that the OIG does not always expect 100 percent recovery of all costs questioned.

Appendix I:

Statistical Information Required by the Inspector General Act of 1978, as amended

Table I.1: Significant Recommendations From Previous Semiannual Reports on Which Corrective Actions Have Not Been Completed

This table shows the corrective actions management has agreed to implement but has not completed, along with associated monetary amounts. In some cases, these corrective actions

are different from the initial recommendations made in the audit reports. However, the OIG has agreed that the planned actions meet the intent of the initial recommendations. The information in this table is based on information supplied by the FDIC's Office of Internal Control Management (OICM). These 48 recommendations from 17 reports involve monetary amounts of over \$21.2 million. OICM has categorized the status of these recommendations as follows:

Management Action in Process: (10 recommendations from 5 reports, \$3.1 million)

Management is in the process of implementing the corrective action plan, which may include modifications to policies, procedures, systems or controls; issues involving monetary collection; and settlement negotiations in process.

The following is a detail of the 10 recommendations (\$3.1 million) related to management actions in progress.

Management Action in Progress:

Report Number: 00-040, Report Title: FDIC Health Benefits Program
Administered by Aetna U.S. Healthcare , Date: September 6, 2000,

Significant Recommendation Number 3: Disallow \$183,100 for overpaid claims
Significant Recommendation Number 4: Disallow \$197,104 for overpaid claims
not collected as contractually required.

Management Action in Progress:

Report Number: 00-040, Report Title: FDIC Health Benefits Program
Administered by Aetna U.S. Healthcare, Date: September 6, 2000

Significant Recommendation Number 4: Continue to research methods of preventing the user community's capability to disable virus protection software used on FDIC desktop workstations and laptop computers without Division of Information Resources Management (DIRM) Information Security Staff (ISS) notification. Once an optimal method is identified, DIRM ISS should implement it on a timely basis.

Management Action in Progress:

Report Number: 01-008, Report Title: Claims Made to the Credit Enhancement Reserve Funds for Securitization Transactions 1992-03 and 1992-04 , Date: March 8, 2001

Significant Recommendation Number 1: Disallow questioned costs of \$401,309 for unallowable costs.

Management Action in Progress:

Report Number: 01-009, Report Title: Securitization Transactions Serviced by PNC Mortgage: Audit of Duplicate Principal and Interest Advances, Date: March

8, 2001

Significant Recommendation Number 1: Disallow duplicate principal and interest payments totaling \$96,359.

Management Action in Progress:

Report Number: 01-007, Report Title: FDIC's Information Technology Risk Management Program , Date: March 14, 2001

Significant Recommendation Number 1: Update the independent security review procedures (ISR) manual.

Significant Recommendation Number 2: Modify the Security Assessment Questionnaire procedure manual to require meetings between the Information Security Section and the user to determine major applications chosen for independent security review. (Funds to be put to better use \$2.2 million).

Significant Recommendation Number 3: Develop new Sensitivity Assessment Questionnaire templates that include an explanation box for each question, and modify the data integrity questions to enhance the reliability of responses.

Significant Recommendation Number 4: Modify ISR procedures to require a meeting between the ISR team and managers before the ISR is initiated.

Significant Recommendation Number 5: Modify the ISR process such that findings outside the control of the user should still be listed in the ISR but clearly identified as to the original ISR and the unit responsible for the corrective actions.

Legal Analysis: (18 recommendations from 9 reports, \$7.1 million)

The Legal Division has been provided all necessary documentation to perform a detailed review for legal purposes. The Legal Division will be the final determinant for items so categorized.

The following is a detail of the 18 recommendations (\$7.1 million) related to legal analysis.

Legal Analysis:

Report Number: 00-024, Report Title: Review of the Claims Made to the Credit Enhancement Reserve Fund for Securitization Transaction 1991-03, Date: July 6, 2000

Significant Recommendation Number 1,2: Disallow \$230,678 in questioned costs for unsupported and unallowable costs related to liquidation expenses, principal and interest advances, and escrow disbursements.

Legal Analysis:

Report Number: 00-028, Report Title: Review of the Claims Made to the Credit

Enhancement Reserve Fund for Securitization Transaction 1991-09, Date: July 21, 2000

Significant Recommendation Number 1,2: Disallow \$1,350,837 in questioned costs for unsupported and unallowable costs related to liquidation expenses, principal and interest advances, and escrow disbursements.

Legal Analysis:

Report Number: 00-029, Report Title: Review of the Claims Made to the Credit Enhancement Reserve Fund for Securitization Transaction 1991-15, Date: July 21, 2000

Significant Recommendation Number 1,2: Disallow \$401,684 in questioned costs for unsupported and unallowable costs related to liquidation expenses, principal and interest advances, and escrow disbursements.

Legal Analysis:

Report Number: 00-031, Report Title: Review of the Claims Made to the Credit Enhancement Reserve Fund for Securitization Transaction 1991-07, Date: August 3, 2000

Significant Recommendation Number 1,2: Disallow \$665,025 in questioned costs for unsupported and unallowable costs related to liquidation expenses, principal and interest advances, and escrow disbursements.

Legal Analysis:

Report Number: 00-032, Report Title: Review of the Claims Made to the Credit Enhancement Reserve Fund for Securitization Transaction 1992-01, Date: July 6, 2000

Significant Recommendation Number 1,2: Disallow \$559,462 in questioned costs for unsupported and unallowable costs related to liquidation expenses, principal and interest advances, and escrow disbursements.

Legal Analysis:

Report Number: 00-034, Report Title: Review of the Claims Made to the Credit Enhancement Reserve Fund for Securitization Transaction 1991-01, Date: August 21, 2000

Significant Recommendation Number 1,2: Disallow \$1,443,836 in questioned costs for unsupported and unallowable costs related to liquidation expenses, principal and interest advances, and escrow disbursements.

Legal Analysis:

Report Number: 00-035, Report Title: Review of the Claims Made to the Credit

Enhancement Reserve Fund for Securitization Transaction 1991-12, Date: August 21, 2000

Significant Recommendation Number 1,2: Disallow \$878,574 in questioned costs for unsupported and unallowable costs related to liquidation expenses, principal and interest advances, and escrow disbursements.

Legal Analysis:

Report Number: 00-041, Report Title: Review of the Claims Made to the Credit Enhancement Reserve Fund for Securitization Transaction 1992-04, Date: September 8, 2000

Significant Recommendation Number 1,2: Disallow \$837,696 in questioned costs for unsupported and unallowable costs related to liquidation expenses, principal and interest advances, and escrow disbursements.

Legal Analysis:

Report Number: 00-044, Report Title: Review of the Claims Made to the Credit Enhancement Reserve Fund for Securitization Transaction 1992-03, Date: September 20, 2000

Significant Recommendation Number 1,2: Disallow \$765,827 in questioned costs for unsupported and unallowable costs related to liquidation expenses, principal and interest advances, and escrow disbursements.

Litigation: (20 recommendations from 3 reports, \$11 million)

Each case has been filed and is considered "in litigation." The Legal Division will be the final determinant for all items so categorized.

The following is a detail of the 20 recommendations (\$11 million) related to litigation.

Litigation:

Report Number: 95-032, Report Title: Local America Bank, F.S.B., Assistance Agreement, Date: March 24, 1995

Significant Recommendation Number 5: Recover \$5,259,285 from the association for noncompliance with the tax benefits provisions of the assistance agreement.

Litigation:

Report Number: 96-014, Report Title: Superior Bank, F.S.B., Assistance Agreement, Case Number C-389c , Date: February 16, 1996

Significant Recommendation Number 1, 4 - 16: Recover \$4,526,389 of assistance paid to Superior Bank.

Litigation:

Report Number: 98-026, Report Title: Assistance Agreement Audit of Superior Bank, Case Number C-389c, Date: March 9, 1998

Significant Recommendation Number 1, 2, 3, 4, 6: Recover \$1,220,470 of assistance paid to Superior Bank.

Litigation:

Report Number: 98-026, Report Title: Assistance Agreement Audit of Superior Bank, Case Number C-389c, Date: March 9, 1998

Significant Recommendation Number 11: Compute the effect of understated Special Reserve Account for Payments in Lieu of Taxes and remit any amounts due to the FDIC.

[Link to Table I.2 - Audit Reports Issued by Subject Area information](#) [this is a link to Section 508 compliant table in html]

[Link to Table I.3 - Audit Reports Issued with Questioned Costs](#) [this is a link to Section 508 compliant table in html]

[Link to Table I.4 - Audit Reports Issued with Recommendations for Better Use of Funds](#) [this is a link to Section 508 compliant table in html]

Table I.5: Status of OIG Recommendations Without Management Decisions

During this reporting period, there were no recommendations without management decisions.

Table I.6: Significant Revised Management Decisions

During this reporting period, there were no significant revised management decisions.

Table I.7: Significant Management Decisions with Which the OIG Disagreed

During this reporting period, there were no significant management decisions with which the OIG disagreed.

Table I.8: Instances Where Information Was Refused

During this reporting period, there were no instances where information was refused.

Appendix II: Products Issued by Corporate Evaluations, Office of Audits

Evaluation Reports - Eval-01-002, August 17, 2001, FDIC's Background Investigation Process for Prospective and Current Employees. Eval-01-003, August 27, 2001, Field Office Cost, Space Utilization, Design, and Usage.

Evaluation Memorandums - EM-01-003, October 24, 2000, Study of FDIC's Corporate Planning Cycle. EM-01-004, November 8, 2000, Study of Internal Control and Internal Review Programs. EM-01-005, March 1, 2001, FDIC's Long-Term Headquarters Housing Study.

Abbreviations and Acronyms

BIF refers to Bank Insurance Fund

BOA refers to Bank of America

CD refers to Certificate of Deposit

CPC refers to Corporate Planning Cycle

CRA refers to Community Reinvestment Act

DCA refers to Division of Compliance and Consumer Affairs

DIRM refers to Division of Information Resources Management

DOA refers to Division of Administration

DOS refers to Division of Supervision

DRR refers to Division of Resolutions and Receiverships

ECIE refers to Executive Council on Integrity and Efficiency

FBI refers to Federal Bureau of Investigation

FDIC refers to Federal Deposit Insurance Corporation

FFIEC refers to Federal Financial Institutions Examination Council

GAO refers to U.S. General Accounting Office

GISRA refers to Government Information Security Reform Act

HHS refers to Department of Health and Human Services

ICL refers to Internal Control Liaisons

IDM refers to Institution Data Management

IRS refers to Internal Revenue Service

ISR refers to Independent Security Review

ISS refers to Information Security Staff

IT refers to Information Technology

MWSB refers to Murphy-Wall State Bank

NPV refers to Net Present Value

OCC refers to Office of the Comptroller of the Currency

OI refers to Office of Investigations

OICM refers to Office of Internal Control Management

OIG refers to Office of Inspector General

OMB refers to Office of Management and Budget

PCIE refers to President's Council on Integrity and Efficiency

PKI refers to Public Key Infrastructure

Results Act refers to Government Performance and Results Act

RLS refers to Receivership Liability System

RTC refers to Resolution Trust Corporation

S&S refers to Spaulding and Slye Colliers

SAIF refers to Savings Association Insurance Fund

TCSB refers to Training and Consulting Services Branch

UR refers to Utilization Rate

Congratulations! The OIG is proud of the accomplishments of OIG staff who were recognized at the Annual Awards Ceremony of the President's Council on Integrity and Efficiency (PCIE) and the Executive Council on Integrity and Efficiency (ECIE) at the National Transportation Safety Board Conference Center on October 17, 2001. Overall, 85 individuals and groups throughout the Inspector General community were recognized for their outstanding contributions toward promoting economy and efficiency in government programs and detecting and preventing fraud, waste, and abuse in federal operations.

Russell A. Rau, Assistant Inspector General for Audits, received a Joint PCIE/ECIE Award for Excellence for his contributions to the federal audit community. Rus was recognized for his leadership in promoting the goals and objectives of the federal audit community during his

tenure as Chair of the Federal Audit Executive Council. One of the key projects that the Council completed under Rus' leadership involved the government's implementation of the President's Decision Directive 63 on Critical Infrastructure Protection.

[Photo of Russell A. Rau, recipient of Joint PCIE/ECIE Award for Excellence.]

An investigations team won an Award for Excellence for Investigations for its leadership and participation in the fraud investigation of the First National Bank of Keystone. Five investigators from our Atlanta Office were recognized for their exemplary service in the federal task force investigating the massive fraud scheme leading to the failure of the bank. Four individuals from the Federal Bureau of Investigation were also recognized for their contributions to the task force.

[Photo of Keystone Task Force left to right- Sam Holland (OIG), Todd Price (OIG), John Micheli (AUSA), Melinda Cash (FBI), Joseph Ciccarelli (FBI), Gaston L. Gianni (IG), Bart Henkle (OIG), Tom McDade (OIG), Phil Robertson (OIG). Not pictured: Gary Sherrill (OIG), Brian Selby (FBI), and Garnett Harris (FBI).]

An evaluations team received an Award for Excellence for its work on the FDIC's nationwide telecommunications contract. Four individuals from our headquarters office were recognized for their analysis and insights on this project. The team's work resulted in significant monetary and program benefits.

[Photo of Evaluations Team- Steve Beard, Ann Lewis, Tiffani Kinzer, Marshall Gentry, Inspector General Gianni]

[Picture of ECIE and PCIE logos]

Offices of Inspector General Report Their Achievements

In August 2001 the President's Council on Integrity and Efficiency and the Executive Council on Integrity and Efficiency released *A Progress Report to the President*, for fiscal year 2000. The report highlights the role the Inspector General community has played in focusing attention on and fostering improvements in the management challenges facing the federal government today and in the near future. Through thousands of audits, evaluations, inspections, and investigations of federal programs and activities, the federal Inspectors General effectively promoted financial management accountability, helped ensure program integrity, minimized risks of fraud and abuse, and produced results. The work of more than 11,000 employees of Offices of Inspector General government-wide during fiscal year 2000 contributed to results that include:

- Potential savings of \$9.5 billion
- Recovery actions of almost \$5.5 billion
- More than 5,500 successful prosecutions
- Suspensions or debarments of nearly 7,000 individuals or businesses
- More than 2,600 civil or personnel actions
- More than 120 testimonies before the Congress on issues of national interest.

[Report cover graphic of Progress Report to the President, by the ECIE PCIE, for fiscal year 2000]

These accomplishments reflect the work of the 57 Offices of Inspector General, whose combined fiscal year 2000 budget totaled about \$1.3 billion.

The FDIC OIG is proud to be a part of the Inspector General community and invites readers of this semiannual report to learn more about OIG activities in other federal agencies by visiting www.ignet.gov.

OIG Hotline

The Office of Inspector General (OIG) Hotline is a convenient mechanism that employees, contractors, and others can use to report instances of suspected fraud, waste, abuse, and mismanagement within the FDIC and its contractor operations. The OIG maintains a toll-free, nationwide Hotline (1-800-964-FDIC), electronic mail address (IGHotline@FDIC.gov), and postal mailing address. The Hotline is designed to make it easy for employees and contractors to join with the OIG in its efforts to prevent fraud, waste, abuse, and mismanagement that could threaten the success of FDIC programs or operations.

[Black and White image of U.S.Flag displayed here]

God Bless America